

# COMMUNIST ECONOMY UNDER CHANGE

**Studies in the theory and practice  
of markets and competition in Russia,  
Poland and Yugoslavia**

**MARGARET MILLER  
TERESA M. PIOTROWICZ  
LJUBO SIRC  
HENRY SMITH**

**What is happening to the economies of the Communist countries? How far do they remain the rigidly state-planned and state-directed economies that the word communism seems to imply? How far has the liberalisation introduced by Khrushchev changed the interior structure of the economies of Russia – and of other communist countries?**

**In short, how “communist” are the communist countries? And how far are they using – or tolerating – economic activity independent of the state and expressing itself in free markets in which buyers and sellers come together spontaneously to exchange goods and services?**

**This book assembles the work of four economists who write independently and with sympathy for the people of the countries they study: Dr. Margaret Miller, a British economist who reads and speaks Russian and knows Russia; Miss Teresa Maria Piotrowicz, a young Pole; and Dr. Ljubo Sirc, a Yugoslav. They describe the economy and the disputations among economists about the form it should take. They draw largely on internal sources for their description and analysis. The book ends with a more theoretical essay on the principles underlying Marxist thinking by Mr. Henry Smith, a leading authority on the economics of Marxism.**

**This book makes a unique contribution to our knowledge and understanding of the communist economies. It will be found absorbing by admirers, sceptics, and those who are neither.**

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## FOREWORD

The publications of the Institute embody the characteristic contribution of the economist to the formation of economic opinion and policy, namely, the study of the interplay of supply and demand in markets. So far, the Institute's full length volumes and shorter studies in the form of the Hobart Papers have mostly<sup>1</sup> analysed the working of markets in commodities, services, labour and capital in Britain, but the analysis of markets is not confined to the free or mixed economies; it can be no less illuminating when applied to state-directed economies. Dr Margaret Miller's study of markets in the Russian economy is the first of its kind.

There have been many economic, political and social studies of the Soviet Union. In this short study Dr Miller has looked at the Russian economy from a new vantage point: that of the degree of economic activity outside the official economic planning machinery of the state. Her knowledge of Russia, its history, people and contemporary literature, rare in English economists, has equipped her to write a review that is not

<sup>1</sup> The exceptions are Colin Clark's *Growthmanship* (Hobart Paper 10, second edition, 1962), Professor J. E. Meade's *UK, Commonwealth and Common Market: A Reappraisal* (Hobart Paper 17, second edition, 1962), and Desmond Donnelly's and Alec Nove's *Trade with Communist Countries* (Hutchinson for IEA, 1960, reissued by André Deutsch, 1963).

only authoritative, original and objective, but also informed throughout by a warm regard for the Russian people.

Too often the Russian economy is regarded, both by its critics and its admirers, as a monolithic state that brooks no activity beyond that which conforms to communist ideology. Dr Miller's study leaves a different impression. In industry, in agriculture, in housing and in trade, in many commodities and services, there is evidence, amply documented from Russian sources, of a large sector of independent private economic activity. And it even penetrates the state sector through *blat*, an unofficial network of inter-state and state/private enterprise dealings which help individual factories to fulfil their plans. All of it is unofficial in the sense that it is not organised by the state; some of it is tolerated by authority; much is frowned on; some is illegal and heavily penalised; but all is evidence of the impossibility of managing an economy of 220 million people from the centre or through local organisations run as executive agents of the centre, and recent moves towards at least partial decentralisation acknowledge this difficulty.

The author relates the tenacity of private effort to the history of the Russian state and the character of the Russian people rather than to the Soviet system established in 1917. Dr Miller believes that the fissiparous tendency of the Russians and the sheer physical difficulties of administering a country of such enormous size with wide variations in climate, natural resources, population and racial composition may make necessary more extensive organisation than for other peoples; but she also believes that the gradual rise in incomes and

the spread of knowledge of the lives of people in western countries will intensify the wish of the Russian people to be allowed wider freedom of choice in their daily lives. And in this she sees a real hope for the future.

In the meantime, the interest for the economist is that, even where the economy is tightly controlled for political or military or other reasons of statecraft, independent economic activity creates markets which cannot easily be suppressed. Indeed, Dr Miller's study suggests that they are tolerated in Russia when centralised control, either for doctrinal reasons or to direct and concentrate production in ways that would not be preferred if left to free consumer choice, has gone too far and has debilitated the vitality of the economy.

The essay on Poland by Miss Teresa M. Piotrowicz is partly based on original sources published in Poland. In broad outline, but with different timing, and with differences in administrative detail, her review of the Polish economy since the end of the war reveals that centralised economic planning faced similar problems to those discussed in the essay on Yugoslavia and has resorted to similar methods of solving them. There also it seems that direction of the economy from the centre encountered difficulties in the allocation of resources and in the absence of incentives. And there too resort has been made to the de-centralised institutions of the market, and, in varying degree, to the use of incentives and inducements employed in western economies.

Since the middle and the later 1950s there has been an approach to the use of markets and to market prices for capital, labour and land. The political purpose of

the Polish regime remains that of collectivisation but there seems to be an increasing gap between the long-term objective and the institutions evolved to contend with the current need to put material and human resources to their most effective uses in the satisfaction of consumer demands. In Poland, as in Yugoslavia and Russia, new economic policies have been freely discussed by economists and their conclusions have been openly accepted in smaller or larger degree by politicians even though they seem to imply the abandonment of the political principles on which communist economies are based and an approach to the principles of the market economies of the West.

Dr Ljubo Sirc traces the official Yugoslav policy on economic affairs, particularly since centralised planning was ended in 1952 and replaced by looser forms of state control using free markets.

His essay thus offers an interesting insight into the efforts made by a small country to work out an economic system that compounds public ownership of material resources, a form of competition between state-owned enterprises, and some freedom for consumers in free markets. It describes one of the few experiments, even though on a small scale and probably unwitting, to test the theories of some socialist economists in the inter-war years who considered that an efficient economy had to rest on the basis of free markets, whether or not there was a large element of state ownership of capital and equipment and state direction of their use. It therefore suggests inferences both for countries that rely mostly on private enterprise and spontaneous co-operation in markets and for those that employ extensive state control.

These essays are followed by a short analysis of communist economic theories of value and development from Marx to the present day by Mr Henry Smith, an authority on the economics of socialism. He argues that Marx's theory of value was fundamentally defective and that fallacies deriving from it persist to this day, both in communist countries and among some socialist thinkers in the West. By purporting to predict the collapse of western society based on free markets these fallacies have inhibited better understanding of the nature of western economy and a readiness by communist leaders to live in peace with it. In more recent times, however, Mr Smith argues that developments in western economic theory are being seen as relevant to communist economy, not least its emphasis on value to the consumer rather than quantity of labour input as the criterion of economic activity. He argues that increasing recognition by communist thinkers of the pertinence of the western economic theory of market value and of the basic stability and rationality of market-based systems, and their application to economic policy in communist countries, offer the prospect that east and west may live together in fruitful competition.

The essays were written independently by the four authors who have no responsibility for one another's work. The Institute does not necessarily accept the analysis or interpretation of events of the authors but believes their studies make a valuable contribution to the discussion of economic policy in liberal and communist economies.

*March 1963*

EDITOR

## BIOGRAPHIES

### MARGARET MILLER

MARGARET MILLER graduated from Edinburgh University with M.A. and B.Com. degrees, and took her Ph.D. at London University. She was for nine years a lecturer in the Department of Commerce at Liverpool University. During the war she was first a research specialist in Soviet affairs at the Foreign Office and later at the Office of Strategic Services (now the CIA) in Washington, where she also lectured on Soviet economics at the George Washington University. After the war she continued her work at the Foreign Office for a year and a half in the Economic Intelligence Department; subsequently she spent 11 years as an administrative officer in the Secretary's department of the Central Electricity Authority (later the Electricity Council).

Dr Miller has travelled extensively in Europe and North America and has visited the USSR seven times, the last in 1961, when she also visited Poland. She is one of the few British economists who can read and speak Russian fluently.

Her published works include *The Economic Development of Russia, 1905-1914* (1926), *Labour in the USSR* (1942), and articles and book reviews in the *Slavonic Review*, the *Listener*, and the *Nation* (New York).

## TERESA M. PIOTROWICZ

TERESA MARIA PIOTROWICZ was born in Warsaw, Poland, but has spent most of her life in Britain. She studied at the University College of Dublin, gaining a Bachelor of Arts in 1960 and a Master of Arts in Economics in 1962.

Noel Coghlan was born in Ireland in 1938. He studied at the University College of Dublin, where he gained a First Class Honours degree in economics, and subsequently at Lincoln College, Oxford.

## LJUBO SIRC

LJUBO SIRC was born in Yugoslavia in 1920. He graduated from the university of Ljubljana in 1943. Thereafter he managed to escape from Yugoslavia, then occupied by the Germans, and joined Tito's army of liberation by a roundabout journey through Italy and Switzerland. He was arrested in 1947 by the Yugoslav government for conspiracy against the State, and imprisoned for seven and a half years. He escaped to Italy in 1955 and made his way to England, where he has worked as a BBC monitor.

In 1960 he took a degree in economics in Fribourg University and thereafter spent a year lecturing at the University of Dacca in Pakistan.

Dr Sirc now lives with his wife in Britain. Since 1962 he has been a lecturer in economics at Queen's College, University of St. Andrews, Dundee.

His publications include: 'Agriculture in Yugoslavia since 1945', *Pakistan Economic Journal*, December 1960; 'Yugoslav Economists on their Country's Economy', *Review of the Study Centre for Yugoslav*

*Affairs*, London, 1961; 'Development of the Communist Economy in Yugoslavia', *ORDO-Jahrbuch*, Munich, 1962.

#### HENRY SMITH

HENRY SMITH was born in 1905. He is one of the foremost British theorists in the economics of socialism.

He began his working life as an errand boy at 13½ and after various jobs in retailing he studied with the Workers' Educational Association and was awarded an extra-mural scholarship to Oxford at the age of 25.

From 1935 to 1937 he was lecturer at the University of Liverpool and then went to Ruskin College, of which he is now Vice-Principal.

The late Lord Keynes formed the habit of sending Mr Smith for his opinion articles on Marxist economics designed for the *Economic Journal*. The late Professor Joseph A. Schumpeter in his *History of Economic Analysis* (1961) said: 'The best analysis of Marx's own views that I know of is that by H. Smith . . .'

Apart from *Retail Distribution: a critical survey* (1937) and his *Introduction to the Study of Economics* (1947), Mr Smith has published a work on *The Economics of Socialism Reconsidered* (1962).

# MARKETS IN RUSSIA

*Margaret Miller*

## **ACKNOWLEDGEMENTS**

I should like to record my gratitude to the Library and Press Library of the Royal Institute of International Affairs (Chatham House) for assistance in compiling the material for this essay, and in particular to Mrs Lydia Bott who is in charge of the Russian press.

I am grateful also to Dr Alec Nove for a helpful discussion on some of the economic issues involved.

M.M.

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## I. HISTORICAL BACKGROUND

### INTRODUCTION

‘... it is the bottom of Russia not the top, the infantry of the country not the cavalry, that has in the long run decided not only the economic but the political life of the state . . . It is necessary to seize from the outset this conception so strongly suggested in the beginnings of Slavonic history, that the history of states may be something very different from the history of peoples, and that, however little chronicled, it is, in the long run, the history of peoples that counts.’

In his perceptive *History of Russia*<sup>1</sup> Sir Bernard Pares points in the above quotation to a vitally important factor in the present relationship between Russia and the West – the gap that has persisted throughout centuries within Russia herself between the small ruling group and the vast masses over whom they hold sway. The broad outline of the development of the Russian state is familiar enough. Cut off from the rest of Europe by the long night of the Tartar domination, the state emerged in the fourteenth century into renewed contact with a Europe that had far outstripped her in cultural and economic progress.

<sup>1</sup> Sir Bernard Pares, *A History of Russia*, Alfred A. Knopf, New York, revised and enlarged edition, 1946, p. 19.

In waging incessant wars to redress this unbalance, the state not only developed its strongly centralised and authoritarian character, but also had to fasten upon the Russian people such intolerable burdens that (as Sir Bernard puts it) they "went underground". There they have remained, their characteristics, aspirations and desires disregarded by their rulers and unknown to the outside world, which has been forced to judge Russia by the face her rulers choose to present.

That face is as disturbing today as it has been at earlier periods in Russian history, but at no time has it been more important to distinguish between official pronouncements and the everyday realities of living among the masses. This is particularly true in the economic sphere, for it is through the people that economic policies must be implemented. The principal aim of this essay is to draw aside at least a corner of the veil that hides these realities, in so far as this can be done by using Soviet sources, and to assess them against the background of Russian history and the work of economists in different countries who study the Russian economy.

#### RUSSIA BEFORE THE FIRST WORLD WAR

The serfdom imposed upon the Russian peasantry presented an obstinate impediment to the growth of market influences. Serfdom was abolished in 1861, but the half-century before the outbreak of the First World War was not long enough to allow a secure start in freeing the economic energies of the people. The great Act of Emancipation, upon which so many idealistic hopes had been pinned, failed to cure either the chronic insolvency of the landed gentry, or the poverty and

land-hunger of the peasants who formed the vast majority of the population. Agriculture worked at a very low level of productivity, held back by the communal system of land-holding, which involved the periodical redistribution of the scattered strips of land among the peasants by the village 'mir', thus discouraging improved methods of farming. The absence of a strong middle class meant that industry and commerce depended heavily on the initiative and financial support of the state, which could be given only by attracting capital, managerial ability and technological help from foreign sources.

Shaken by the 1905 revolutionary movement, the government introduced reforms in agriculture, associated with the name of Stolypin, the Minister responsible for implementing them. These changes recognised the slowly growing differentiation in the Russian village into the poor, 'middle', and wealthy (by Russian standards) peasants, and set out to encourage the latter. Stolypin was 'betting on the strong', by giving to the more go-ahead and successful peasants the right to withdraw from the village commune and have their scattered strips consolidated into individually-owned holdings. About a quarter of the peasants took advantage of these provisions in the brief period between 1906 and 1913. An urban development worth mentioning in this connection was the rapid growth of small deposits in the Savings Banks, testifying to at least the beginning of a lower middle class in Russia, comparable with the 'small shop-keeper' class in Britain.

#### WAR COMMUNISM, 1917-1921

To what extent this 'wind of change' would have

enlivened Russia's immature economy and encouraged the growth of private enterprise cannot be known, for the hurricane of total war swept it away in a few years. The Bolshevik government inherited a badly run-down economic machine, and the further losses caused by civil war and foreign intervention, aggravated by the doctrinaire economic policies pursued by the government, not only destroyed the last vestiges of economic freedom but brought the country to the verge of collapse. The government's dilemma was how to deal with the discontent both of the peasants and the town workers. The peasants were angered by the forced requisitions of their produce which the government found necessary to support the Red Army and feed the towns. Left with barely enough for their subsistence and nothing for the market, the peasants retaliated by reducing their output. The workers were alienated by the consequent food shortages, and demoralised by the shut-down of factories for lack of raw materials. Money was rendered valueless by massive inflation. Labour was conscripted and sent from place to place to undertake essential jobs. Early in 1921, the Kronstadt revolt forced the government to realise that a strategic retreat was unavoidable.

#### THE NEW ECONOMIC POLICY, 1921-1928

Once again, by one of the violent swings characteristic of Russia's history, the forces of the market were released. The peasants were allowed to sell any surplus they had left for whatever prices they could get after surrendering a smaller part of their produce to the state. The state retained its hold over the 'commanding heights' of the economy, large-scale industry, finance,

transport, while allowing some revival of private enterprise in other sectors. Even during the period of war communism private trade had been carried on illegally by 'bagmen' who moved between the country districts and the towns bartering grain for consumer goods. In the early years of the New Economic Policy (NEP) private merchants quickly took over about three-quarters of retail trade, and private enterprise flourished in the wholesale trade. In industry many small plants were leased to co-operatives and private operators: some were handed to companies, using both state and private capital; others were leased to foreigners who ran them on concession. These private concerns were small, and owing to the uncertainties of the time statistics have to be handled with caution. Small-scale industry may have accounted for one-third of industrial employment towards the end of the NEP period.

A new rouble was introduced and money restored as the basis of economic relationships. Markets for all commodities were reinstated, and in Moscow and other cities financial exchanges were organised for buying and selling government bonds and foreign currencies. The privately-directed energies released in this way were remarkably effective, and by 1926 the country's economy was restored to the 1913 level.

Thereupon the government was faced with a new dilemma in carrying out the aims of the Revolution. Could it allow private enterprise to continue to flourish in the countryside in the shape of over 25 million independent farms, while building socialism in the towns on state-planned and state-controlled industry? After lengthy debate, the decision was taken to reject the market principle and to substitute force as the guiding

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factor in economic development. 'The market approach must be rejected,' said Kuibyshev, head of state planning. 'The market situation can be one current, but a Communist and Bolshevik has always been able, and is able, to swim against the current'.<sup>1</sup>

### 1928 ONWARDS: THE FIVE-YEAR PLANS

In yet another costly reversal of policy, the peasants were compelled to join collective farms, precipitating a grim and desperate struggle which left in its wake a trail of physical and psychological damage not yet outlived. By 1931 the very class upon whom the Stolypin reforms had relied for their success had been forced out of existence, as had the private small-scale manufacturers and traders. But the government had secured what it needed, the power of direction over agricultural production, and was free to go ahead with industrialisation through its five-year plans.

There is general agreement among students of Soviet economics that the hectic pace of development imposed heavy sacrifices on the Russian people. There is much disagreement, inevitable in view of the difficulty of ascertaining the facts about Soviet economic activities, about the degree of efficiency with which planning has done the job, and whether other methods would have been more efficacious. Some hold that a slower rate of development, with more attention paid to consumer needs, would have yielded better results from the strictly economic point of view. On the broad effectiveness of the industrialisation drive in achieving the

<sup>1</sup> 'Some Soviet Economic Controllers', in *Soviet Studies*, Quarterly Review of the Social and Economic Institutions of the USSR, Vol. XII, July 1960 (Basil Blackwell, Oxford).

politically-inspired aims of the government there can be no doubt. Even before the war the results were spectacular. Thousands of new factories, power stations and mines were built. Production of coal, iron, steel was quadrupled, supplies of electrical energy multiplied. New industries came into being, for example, making lorries, tractors, machine tools, heavy chemicals, plastics. Immense progress was made in acquiring industrial skills, and the non-agricultural labour force increased to about 30 million, three times larger than in 1928. Industries were redistributed geographically to make better use of raw material and transport, and to lessen dependence on the strategically vulnerable western areas. After an interval to repair the ravages of war, progress was resumed at the same breakneck speed, and with the same emphasis on heavy industry, current targets being enshrined in the Seven-Year Plan (due to end in 1965) and the directives for 1960 to 1980 given at the 1961 Congress of the Communist Party. Although backward agricultural Russia has long since been transformed into the second largest industrial power in the world, she still thinks it necessary to make immense efforts to overtake her one remaining rival, the United States of America.<sup>1</sup>

<sup>1</sup> A full treatment of this historical background will be found in: Margaret Miller, *The Economic Development of Russia, 1905-1914*, P. S. King and Sons, London, 1926; Maurice Dobb, *Soviet Economic Development since 1917*, Routledge and Kegan Paul, 1948; Harry Schwartz, *Russia's Soviet Economy*, Jonathan Cape, 1951.

## 2. PLANNING

### OUTLINE OF THE SYSTEM

Having thrown out the market principle, the Soviet authorities had to set up something in its place; that something was central planning. Where we in the West look to the forces of demand and supply and consumer pressures to regulate economic relationships, the Soviet leadership believe in a 'command' system, with its apex at the highest seat of political power and its base at the individual firm, factory or farm. The system had its beginnings as early as 1920, while the civil war was still going on, in GOELRO, the state commission for electrification, established to prepare an electrification plan for the whole country. In the prevailing conditions of economic disorder these early planning efforts could be only tentative, and in the following year the commission was merged in a larger body, the state planning commission, or Gosplan, which, with many changes and reorganisations, has survived to this day as a committee of the Council of Ministers. This government body, and the all-powerful Central Committee of the Communist Party (or, more accurately, the small controlling groups within these bodies), constitute the supreme ruling forces in the country.

Extending the planning controls over such a rapidly

growing economy was necessarily slow and difficult. In a very simplified form the process is as follows. The political leaders issue general directives on the lines that economic development is to follow in the next planned period. Gosplan works on these directives to relate them to the economic capabilities of the country, and to co-ordinate the different branches of the economy. Then through Gosplan's regional offices they are passed to the Commissariats (changed to Ministries after the war) which control the different branches of industry and other sections of the economy. From there they flow through the Chief Administrations (Glavki), to the smaller groupings called trusts and combines, until they reach the individual enterprise. At all stages of this hierarchical progression the directives are scrutinised by the Republican and local Communist Party committees, and worked on by the people ultimately responsible for carrying them out, and who know what resources of labour, machinery, materials and money will be required to achieve the planned targets. Thus the directives gain in precision and reality before their backward flow through the same channels to the centre, where they receive final confirmation by the political power and are issued as instructions legally binding on all concerned. In theory every economic unit carries out the orders of its superior organisation, and the processes of plan fulfilment are subject to specific check at all stages by bodies like the State Bank, the Central Statistical Committee and others, as well as by the local Party committees.

It is a firmly held belief of communist dogma that planning is immensely superior to the system of free enterprise. Here is the magic formula by which order

and stability are introduced into economic life. It makes possible the fullest and most rational use of economic resources and permits a rate of development beyond the reach of capitalist countries with their chaotic economies bedevilled by alternate booms and slumps.

#### SHORTCOMINGS OF PLANNING

Opinions behind the scenes, in the give and take of everyday debate, are very different. An eminent Soviet economist is quoted as criticising the 'chronic rigidities and bottlenecks' of planning and maintaining that the crudity of Soviet planning techniques has accounted for a waste of anything from a quarter to a third of potential output.<sup>1</sup> The 22nd Congress of the Communist Party in October, 1961, produced a crop of speeches from high-ranking officials criticising various aspects of planning. It failed, it was said, to encourage the adoption of new techniques in industry,<sup>2</sup> a vital point underlined by Mr Khrushchev himself on the same occasion, when he expressed the urgent need for a forward - moving and dynamic economy in one of his pungent folk-sayings, 'You can't jump high fences on an old horse' ('Na starom konye vysokykh baryerov nye vozmyesh').<sup>3</sup> Further defects of planning freely aired in the press were its failure to ensure the requisite standards of quality in industrial products

<sup>1</sup> Alfred Zauberman, 'New Winds in Soviet Planning', *Soviet Studies*, *op. cit.*

<sup>2</sup> Speech by I. V. Spiridonov, First Secretary of the Leningrad Oblast Party Committee, to the 22nd Congress of the Communist Party, *Pravda*, 20 October, 1961.

<sup>3</sup> Report by N. S. Khrushchev to the Congress, *Pravda*, 18 October, 1961.

and to encourage specialisation, even when specific proposals towards these ends had been made.<sup>1</sup>

Occasionally the hard-pressed planners hit back at their critics, claiming that it was not much use drawing up careful production plans if the industries concerned failed to implement them, or did so with long delays.<sup>2</sup> This speaker went on to deplore 'localism' ('myestnichestvo') among industrial enterprises, who persisted in putting up large numbers of 'their own' small shops for manufacturing building materials, in defiance of the national plan. The failure of state planning to secure the subordination of local to national interests drew angry words from Mr Khrushchev, when he belaboured industrialists in Dnepropetrovsk, Briansk and Uzbekistan for over-spending on materials and equipment for the benefit of 'their' areas, again at the expense of plans drawn up at the centre for the planned development of the whole country.<sup>3</sup> The principle on which they worked, expressed in the Russian saying, 'Nu, kak nye poradyet rodnomu chelovyeku?' ('Blood is thicker than water'; literally, 'Now, how can one refuse to help a close friend?') was, he declared, a 'shocking breach of state discipline'.

An editorial in *Izvestia* took up the same theme,

<sup>1</sup> A. Veimer, 'Plan, Co-operation, Deliveries', *Izvestia*, 19 May, 1961.

<sup>2</sup> Speech by V. E. Dymshits, First Deputy Secretary of Gosplan USSR, in which he says that the government's plans for housing construction are being held up because of delays all over the country, running into years, in building factories to turn out baths and other necessities. In Kazakhstan not a single such factory had been built despite planning instructions, and the goods had to be hauled thousands of kilometres from other parts of the country.—*Pravda*, 28 October, 1961.

<sup>3</sup> *Pravda*, 18 October, 1961, *op. cit.*

emphasising the impossibility of supervising the economy from the centre, now that it had grown enormously in size and complexity.<sup>1</sup> The system could work well only if everyone, including factory managers and workers at the bench, understood that the interests of the state and of their enterprises were identical. An example was given in which cranes produced for large industrial enterprises could not be used because another factory scheduled to produce motors for them had failed to deliver. The defaulting management declared that the planning organs had put supplementary work on to them, without indicating priorities, so 'how were we to know what to do first?' This attitude was condemned. 'State discipline' demanded that the management should have assessed the situation in the light of national interests and not of their own convenience, in which case they would have given priority to the production of motors. Similarly the deputy chairman of the Volgograd city executive committee was rebuked for infringing state discipline by assigning space for office buildings, at a time when the government had put a temporary stop to such building in favour of the construction of shops and houses.

The heaviest attacks on planning centred on its long-standing inability to co-ordinate inter-regional supplies. This failure was frequently associated with the tendencies to local autarchy noted above, and was particularly significant in a country the size of Russia. An article in *Izvestia* was concerned with the heavy losses it imposed on the economy by prolonging the time set for building new enterprises and thus raising

<sup>1</sup> 'Concerning State Discipline', 27 January, 1962.

the costs of getting them into production.<sup>1</sup> The writer went on to emphasise the impossibility of keeping industrial output flowing smoothly if essential supplies were not forthcoming at the planned times. The operations of the machine-building and tool-making factories in Estonia provided an illustration. Supplies were needed from no fewer than 150 enterprises in 45 different economic regions, merely in order to satisfy the needs of the departments in the industries producing radio-technical and telephone apparatus. Gosplan would have to keep to a much more reliable schedule if improvements were to be effected, and the writer put forward a specific programme to which he thought the planning authorities should adhere in approving plans submitted to them.

Mr Khrushchev also high-lighted this question of building delays in his speech at the 1961 Party Congress, saying that there were more than 100,000 projects under construction, and many of them were coming into production two or three years later than the planned times, thus freezing enormous amounts of state funds. A year's moratorium on new building had had to be imposed.

#### RECENT ORGANISATIONAL CHANGES

These are serious criticisms, even allowing for the well-known Russian passion for self-criticism ('samo-kritika'). It is also significant that the authorities have never ceased to tinker with the mechanism of planning since it was first set up. Before and after the war plan-

<sup>1</sup> 'Uninterrupted planning—the guarantee of success', by P. Lomako, Chairman of Krasnoyarsk Regional Economic Council, 11 April, 1961.

ning bodies were constantly subjected to administrative reorganisations. Leading personalities were shifted around or removed with high frequency. The pattern of incessant change culminated in Mr Khrushchev's reforms of 1957, the most sweeping revisions in industrial administration since the Revolution. Most of the Ministries were wiped out, and the vertical system of control of industry was replaced by a territorial system vested in over 100 regional economic councils (sovarkhozy). The basic purpose was to get rid of the top-heavy over-centralised system of planning and administration centred in Moscow, and devolve decision-making to the localities, but keep the levers of economic power – finance, investment, control over supplies of key commodities – firmly in the hands of the central government, and trust to the support of the local Party officials. After a few years' experience, it was apparently thought that decentralisation had gone too far, for in April 1961 a measure of re-centralisation was introduced. The country was divided into 17 economic regions and new councils were set up in them to co-ordinate and plan the work of the sovarkhozy.<sup>1</sup>

Extensive as they were, the reforms did not change the hierarchical nature of industrial administration. The sovarkhozy, which are roughly comparable to the former glavki, have the duty of supervising the fulfilment by the enterprises subordinated to them of the plan laid down by higher authority. They are in turn responsible to the Gosplan of the Republic in which

<sup>1</sup> S. Tokarev and P. Alampiev, 'Questions of improving the territorial organisation of the national economy and economic division into districts', *Planned Economy* ('Planovoye Khozyaistvo'), No. 7, 1961. See also the relevant chapters in Alec Nove, *The Soviet Economy*, George Allen and Unwin, 1961.

they are situated, and through them to the Union Gosplan. The first effect of the 1957 reforms was a large increase in the powers of this body, which acquired most of the functions of the dissolved Ministries. A decree of April 1960 modified the situation somewhat by expanding the activities of an existing body, the Economic-Science Council (Gosekonomsoviet), to enable it to deal with long-term planning problems, while giving Gosplan the duty of attending to the current planning period which extends five years forward.<sup>1</sup>

#### RETURN TO ECONOMIC RATIONALITY?

This ceaseless barrage of criticism and argument, and the frequent organisational changes, indicate that 'swimming against the current' is a strenuous undertaking and in recent years there have been signs that many of Russia's economists, mathematicians and practical planners want to reintroduce some of the automatic regulators of the market mechanism in the interests of greater rationality. This, however, runs counter to established dogma.<sup>2</sup> Interest on capital and rent for land cannot be reconciled with the Marxist doctrine that labour is the sole source of value. According to official belief, prices can be settled by administra-

<sup>1</sup> All the reference books on general economic development listed on p. 255 give detailed descriptions of the growth and functioning of the planning system. See especially Alec Nove, *op. cit.*, Chapter 2, 'Administration, Planning, Policy Decision', and Chapter 7, 'Planning and Investment'.

<sup>2</sup> L. Illichev, 'A powerful factor in the building of communism', *Kommunist*, No. 1, January 1962. The author rebukes the Soviet economist L. Leontiev for advocating such ideas, which amounted to 'throwing out of economic science the basic law, and also other laws, of the political economy of socialism . . .', thus 'throwing doubt upon the whole political economy of socialism.'

tive action and not by the pressures of demand and supply. Little regard, it was thought, need be paid to the settling of realistic depreciation rates in a planned economy.

These ideas could be held more easily in the early years of the planned period, when political domination and coercive methods could be used to achieve the desired aims without undue economic loss. But the very success of industrialisation established an economy the administration of which could no longer be confined within the former narrow limits without an unacceptable degree of loss and inconvenience. Hence the recent tendency for some 'capitalist' concepts to make their way back into the economy, sometimes in disguised form. For example, the need to direct investment into its most productive uses has been compelling the practical planners to seek for some measure by which alternative uses of capital could be compared: hence the growing use of formulae permitting what is in fact an interest rate to be applied, although it may be called the 'pay-off period', the 'recoupment period', ('srok okupaenosti') or some such ideologically harmless term. The latter simply meant finding a principle upon which scarce capital resources could be directed to their most efficient use from the point of view of the economy as a whole. One project might need more capital investment than another, but would save on current costs, and 'pay off' the additional capital in ten years. Another project might 'pay for itself' in this sense in eight years. Other things being equal, the project with the shorter pay-off period should be preferred.

The urgent need to streamline planning techniques,

and the advent of the electronic computer, are making possible the adoption of new, less arbitrary, and more efficient price-fixing techniques, and much more attention is being paid to obsolescence.<sup>1</sup> To secure increased flexibility, plans are no longer to be static for the planned period, but are to be revised every year and are to include targets for the major indicators five years ahead.<sup>2</sup>

The current debate about planning methods clearly indicates the growing recognition within the Soviet Union that methods applicable to the earlier stages of industrialisation, when the 'laws' of economics were swept aside by the politically-inspired decision to industrialise as quickly as possible at any cost, are no longer suitable for an economy that has grown enormously in size and has become more mature and vastly more complex than it was 30 years ago. Planning has indeed been successful as an instrument for bringing about enormous increases in production, starting from very low levels, making the utmost use of advanced technological achievements in the West, and drawing upon a huge reservoir of surplus labour in the countryside. But it has not solved the quite different problem of fitting together in an immensely complex pattern the intricate economic inter-relationships between all the

<sup>1</sup> R. W. Campbell, *Soviet Economic Power*, Houghton Mifflin Co., 1960. See also *Value and Plan*, edited by Gregory Grossman, University of California Press, 1960; Alec Nove, *op. cit.*, pp. 211-214; R. W. Campbell, 'Some Recent Changes in Soviet Economic Policy', *World Politics*, Vol. IX, No. 1, October 1956; Gregory Grossman, 'Economic Rationalism and Political Thaw,' *Problems of Communism*, Vol. VI, No. 2, March-April 1957.

<sup>2</sup> Naum Jasny, 'Stages of Soviet Economic Development', in *Survey*, a Journal of Soviet and East European Studies, No. 37, July-September 1961.

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undertakings and organisations engaged in translating paper directives into the realities of steel, paper, bricks, and the thousands of other commodities needed in a modern and increasingly sophisticated society.

### 3. INDUSTRY

#### BLAT: THE SHADOW SYSTEM OF PRIVATE ENTERPRISE WITHIN PLANNING

While politicians and economists argued endlessly about theory, the men who have to get the job done have been quietly dealing with this problem in their own way ever since planning began. Over-ambitious plan targets, internal inconsistencies between plan indicators, value, quality, assortment, etc., all of which could not simultaneously be met, chronic shortages of materials with which to meet plan targets, the mistakes and imperfections of planning techniques: all these had to be faced in everyday life by plant managers, directors, administrators, accountants and the like. Immense emphasis has been laid on plan fulfilment by the authorities, and failure to secure it carried heavy penalties, perhaps dismissal, with the loss not only of salary but also of the 'fringe benefits' associated with a responsible position in industry: housing, the use of a car, access to holiday resorts. There was even the danger of being accused of 'sabotage' and facing criminal charges. To meet these pressures, the practical men have evolved a system of self-help and mutual defence, and this finds shape in an unofficial network of inter-enterprise relationships.

Perhaps the most pervasive element in this network is 'blat', which can only be described in English by some such term as 'the old boy network'. It means using personal influence or contacts to obtain favours or concessions to which the individual or business is not entitled by law. Its prevalence reveals itself in such sayings as 'blat vyshe Stalina' ('blat is higher than Stalin'), or 'blat vyshe Sovnarkoma' ('blat is higher than the Council of Ministers'). It permeates the whole system of planning, from the time when the broad general directives are passing down the industrial hierarchy and back again to the centre. This process gives time and opportunity for conferences and discussions between the higher economic bodies and the undertakings subordinate to them, in the course of which 'blat' can be, and is, extensively used to lessen production tasks, increase allocations of essential materials, and bring the plan within the capacity of the producing unit, as seen by the officials who will be responsible for fulfilment. Even if this is done with complete success – and of course it may not be, since the higher organs are aware of the tendency of their subordinate bodies to include some 'fat' in their claims and may trim some of it off – crises and shortages of various kinds that imperil plan fulfilment and demand the exercise of 'blat' are bound to be met in the day-to-day work of the business. The procedure has to be conducted with skill, as mistakes are penalised heavily. Thus the director of a machine-building factory, Tkachenko by name, was dismissed after it was discovered that he had supplied other factories with products of his own works, not on the basis of an official 'order' ('naryad') on which alone goods can legally be

supplied, but simply on grounds of personal friendship with the directors of the consuming factories.<sup>1</sup>

The 'tolkach' ('pusher', 'expediter') assists industrialists in dealing with their most difficult problem, that of securing supplies. These specialised middlemen make it their business to know where supplies can be obtained, and may work on a commission basis for several undertakings, or may be carried on the books of one business as 'special representatives'. No one knows how many are employed in this way, but there are indications that their number is large. One authority mentions no fewer than 8,000 'tolkachi' descending on a single regional economic council at one time. It has been estimated that many firms get a quarter to a half of their supplies through unofficial channels, relying largely on the services of 'tolkachi'.<sup>2</sup>

High planned targets are responsible for another constant tendency (insurance, 'strakhovka') on the part of management to build up stocks of materials and thus preserve an essential element of slack, which will enable them to cope with unexpected demands or shortages. Some of these materials eventually find their way on to the free market, which serves as the basis for the work of the 'tolkach'.

If all else fails, the manager may resort to 'simulation' ('ochkovtiratelstvo') to make it appear that he has fulfilled the plan, by using various devices: producing the wrong assortment of goods, manipulating the accounting of goods in process, lowering the quality of output, and so on.

<sup>1</sup> *Izvestia*, 27 January, 1962, *op. cit.*

<sup>2</sup> Alec Nove, *op. cit.*, p. 202; Joseph S. Berliner, *Factory and Manager in the USSR*, Harvard University Press, Cambridge, Mass., 1957, p. 222.

All these practices are familiar targets for criticism in the Soviet press, but they continue because not only the manager's professional reputation and his job depend on them but also his remuneration. Apart from his basic salary, he receives generous bonuses for fulfilment and over-fulfilment of his production tasks, and as they may double his salary, and commonly increase it by at least 30 per cent, as well as influence the amount he may distribute in bonuses to his staff, they constitute a powerful incentive to plan fulfilment, even by unofficial channels and methods.

#### BLAT IN ACTION: REPORTS IN THE PRESS

Plant managers and administrators are not people who write much about their jobs, especially about the elements in them that are, strictly speaking, outside the law. Hence press references are frequently indirect, but are illuminating none the less. One article told of the author's surprise at meeting a group of skilled engineers in the hotel at which he was staying in Tyumen, east of the Urals, near Sverdlovsk.<sup>1</sup> They had made the long journey from Leningrad and Nikolayev because their ship-building firms had been unable to secure delivery of essential supplies – in this case winches – on order from a factory in Tyumen. The factory manager excused his failure to deliver on the ground that these items constituted an 'insignificant percentage' of his total production, and were therefore given only a corresponding amount of his attention. Meanwhile expensive passenger liners, tankers, fishing vessels, ice-breakers, were being held up, and time was being lost by highly trained specialists who had to be

<sup>1</sup> Ilya Omelichkin, 'Icy Silence', *Izvestia*, 30 November, 1961.

taken off their jobs to act as 'tolkachi'. In this case the delinquent manager lost his job, but there was no record of similar action being taken in equally lengthy delays reported in the same article from a factory in Kiev. In another case, an enterprising 'tolkach', apparently self-employed, extracted 400 wagon-loads of precious timber from a supply organisation in Moscow, and re-sold them to five state farms at a handsome profit. According to the report, the directors of the farms had just not bothered to ascertain the whereabouts of the supply organisation in Moscow, and the 'tolkach' was able to cash in on their inertia.<sup>1</sup>

Another writer directed attention to the harm that could be done to the economy by the wrong use of the system of premiums.<sup>2</sup> He described how he had watched two young girls unloading bricks from a lorry in a Moscow street and doing the job in such a hurry that 30 per cent of the bricks were reduced to rubble. Evidently the girls, as well as the lorry driver and the freight-carrying organisation behind them, were paid bonuses depending on the amount of work done; hence the rush to finish as quickly as possible. The economy as a whole would have benefited if they had carried fewer bricks at a lower spoilage rate, but incentives based on quantity led to the sacrifice of quality. He deplored not only the economic loss but also the moral loss inflicted on the workers by the resulting conflict between lofty appeals on the one hand and the demands of plan fulfilment and material

<sup>1</sup> Kamil Faizulii, 'The Timber Magician', *Literaturnaya Gazeta*, 11 January, 1962.

<sup>2</sup> 'For all and for oneself', by O. Antonov, Member of the Supreme Soviet of the USSR, *Izvestia*, 22 November, 1961.

self-interest on the other. Correspondence evoked by this article emphasised that bonus systems evolved at a time when factories were badly equipped and workers were unskilled, harmed the economy in conditions of growing automation and a much higher level of skill among workers and managers. The net effect was to introduce a general 'go-slow' tendency throughout the industry, when a garment factory which had achieved 99 per cent first quality work found that, because of the bonus system, its material rewards were less than those of a factory whose proportion of first-class work was only 80 per cent but which was able to show improvements each year.

#### SIGNIFICANCE OF THE SYSTEM

A system of this kind does not lend itself to accurate evaluation, and opinion outside the USSR swings from the point of view that the whole machinery of economic life would collapse if these 'private enterprise' activities were withdrawn,<sup>1</sup> to the suggestion that they represent the

'severely harnessed rudiments of a market economy seeking to break through the hard crust of centralised planning'.<sup>2</sup>

The relative absence of condemnation from official circles can be explained by their usefulness, first in securing the achievement of planned targets and lessening the economic losses inherent in the admitted crudities of planning techniques, and secondly by the

<sup>1</sup> Paul Barton, 'The myth of planning in the USSR', *Saturn*, Vol. III, No. 1, January–February 1957. (Paris, International Commission against Concentration Camp Practices.)

<sup>2</sup> Joseph S. Berliner, *op. cit.*, p. 206.

fact that they can be made to appear ideologically acceptable as 'exercising initiative', the working of 'democratic centralism', or the means by which local initiative is reconciled with control at the centre.

The temptation to use them for private gain is, of course, always present, and the practices can quickly degenerate into theft, pilferage, or deliberate falsification of accounts. The latter have always been widespread in the Soviet economy, in spite of incessant propaganda aimed at persuading people to protect state property as they would their own. They are apparently increasing, to judge by the restoration of the death penalty in May, 1961 for currency speculators, embezzlers, forgers, people who steal public property and other offenders. The law was extended at the end of February, 1962 to cover certain cases of bribery, described as one of the most vicious 'relics of capitalism'.<sup>1</sup>

For this study of the Soviet economy, the special interest of these unofficial activities is that they reveal the extent to which the rigidities of an authoritarian economy and a centralised planning system geared to the rapid increase of production totals are softened by the hidden pull of market forces, and give a picture of economic motivation among the managerial class and the workers they control. They show Soviet men and women to be actuated by much the same motives as their counterparts in capitalist countries: the need to earn a living; the desire to do so while avoiding undue strain and getting the maximum remuneration for the minimum effort; the habit of

<sup>1</sup> *Gazette of the Supreme Soviet of the USSR* ('Vyedomosti Verkhovnovo Sovieta S.S.S.R.'), No. 8 (1095), 21 February, 1962.

putting their own interests before the common good when the two come in conflict. Of course there are other motives: devotion to the job, the desire to do well, to have a successful career, to make the best use of one's training, to exercise initiative and authority, loyalty to the ideals of the state; but it would be difficult to prove that these are any more common in the Soviet Union than they are in free enterprise societies.

### POSTSCRIPT

#### FORWARD TO FREE MARKETS ?

During the two months before the meeting of the Central Committee of the Communist Party in November 1962, a remarkably outspoken newspaper campaign in *Pravda* brought to a head the long-standing dissatisfaction with the planning system. The campaign was initiated by Professor Ye. Liberman of the Institute of Engineering and Economics at Kharkov University. His main thesis was that the undue emphasis given by the planners to quantitative plan fulfilment was responsible for the universal tendency among industrialists to strive for an 'easy' plan ('blat'), to hold unnecessarily high stocks of materials and equipment, to hoard labour ('strakhovka'), and to seek fulfilment of quantitative indices at all costs, even if it meant penalising go-ahead workers and businesses as compared with the less efficient, ignoring technological advance and 'cooking the books' ('ochkovtiratelstvo').

The main corrective suggested by the originator of what has come to be known as the 'Kharkov system' was to link the factory's rewards not to the increase in gross production over the previous year but to the

profits earned on its capital assets. Every plant should create an incentive fund into which payments would be made on a national sliding scale depending on the ratio of profits to capital, and out of which staff premiums and bonuses would be paid, machinery purchased, and normal extensions and improvements to the factory financed. As a result, industrialists would have a material incentive to maximise their profits and hence their incentive funds. It would also be no longer to their interest to hold large stocks of materials or to hoard labour. Once they had to pay the equivalent of a rate of interest for new plant and equipment instead of receiving them as a free grant from the state, they would economise in their use.

Other planning practices which the 'Kharkov system' aimed at liquidating were: the excessive degree of administrative control of the individual enterprise by planners who were too remote to know about its capacity or the needs of the consumers who used its product; and the 'departmental approach' of the planners, who worked on different indices of the plan – quality, value, cost of production, assortment, productivity of labour – without co-ordinating the final results, thus forcing industrialists to work on plans that were unrealistic and internally inconsistent.

At first sight Mr Khrushchev's speech at the Central Committee gave little encouragement to these bold proposals. Most of his attention was devoted to political and Party aspects. The Party itself was reconstructed from top to bottom and split into two sections, one to concentrate on industry, the other on agriculture. The system of governmental control was consolidated by merging the two existing bodies into a single Committee

of Party-State Control which, with its branches, was to assist the reorganised Party in carrying out its new assignment in economic management. In industry, to which the reforms were specially directed, the key-note was recentralisation, and this to a large extent nullified Mr Khrushchev's 1957 measures of industrial decentralisation. Centralised research committees were to be set up for each branch of industry in the hope of speeding up the adoption of new techniques. Capital construction work into which the government was pouring massive funds was similarly reserved to the central power to combat tendencies to autarchy and widespread economic waste. The hundred or so regional economic councils ('sovnarkhozy') set up in 1957 were increased in size and drastically reduced in numbers, bringing about a high degree of recentralisation in industrial management.

A closer scrutiny of the speech, however, reveals that, in fact, all the Liberman proposals have received official sanction, although they are to be put into practice only gradually and experimentally. Central planning has been streamlined by moving the centre of gravity in planning away from Moscow to the republics, and central organs will confine themselves to long-range planning and to welding the separate plans into one national plan. The 'sovnarkhozy' and the enterprises have now the prospect of more freedom in running their affairs within the general framework of strongly reinforced Party controls. Detailed planning from above will stop at regional level. Thereafter the enterprises themselves will draw up specific plans in the light of their known resources, after ascertaining the needs of the people. Demand and supply will be brought

together at the level of performance *before* plans are approved from above. Plant managers will have authority to vary the plan during the year if thought necessary, and will have increased powers to 'hire and fire', to confine premiums to workers who have contributed to increased productivity, and to put pressure on suppliers who fail to deliver on time. The duty of the 'sovmarkhоз' will be to co-ordinate enterprise plans with regional and national requirements. Mr Khrushchev specifically accepted that profit was an indispensable yardstick by which to measure the level of efficiency in individual businesses, and that economists and planners should work out the ways in which it could most advantageously be applied throughout industry.

These planning and managerial reforms in industry are immensely complex, and it is too early to see how they will be worked out in practice. There is no guarantee that their implementation may not be held back or distorted by the entrenched power of bureaucracy and the reinforced authority of Party functionaries. But in one form or another they are bound to go forward. Even at this early stage they are a striking vindication of the pressures described above: from economists and practical planners for more rationality in economic thinking and freedom from the dead hand of political dogma; from industrialists and business men for plans which correspond to the realities of available resources, for freedom from bureaucratic control in the everyday conduct of their affairs, and fewer administrative barriers between producers and suppliers; and from consumers who, with rising prosperity, are demanding a wider range of better quality goods.

March 1963

M. M.

## 4. AGRICULTURE

### THE PRESENT SITUATION

Two things stand out in the present agricultural scene. In spite of the severe discouragement of private markets by collectivisation over 30 years ago, about half the meat and milk, nearly all the eggs, and much of the fruit and vegetables consumed by the Russian population still come from the private sector, the small private plots which the collective farmers cultivate for their own use. Visitors to Russia have long known that if they cannot find cheese, or fresh fruit, or butter in the state shops, they can be sure of being able to buy them – at a price – in the kolkhoz markets which exist in every town. The other striking fact is that, in contrast to the spectacular achievements in industry, agriculture has consistently lagged behind, and production totals have remained disappointingly static.

### RECENT CONCESSIONS

Following the death of Stalin in 1953 steps were taken to improve this situation, in the first place by increasing incentives for the producers. The prices of agricultural products bought by the government from the peasants were raised, and the prices of industrial goods supplied to them were reduced. Capital investment in agricul-

ture was also substantially increased and, as in industry, planning was decentralised so as to give the farmers themselves more elbow-room in making decisions.<sup>1</sup> In 1958 the government took the important step of disbanding the machine-tractor stations, through which they had exercised control over plan fulfilment in agriculture, and allowing the collective farms that had the necessary funds to buy up the stocks of agricultural machinery for their own use. It was hoped that combining the land and the machinery to work it in the hands of the same people would prove a powerful stimulus to agricultural production. Western observers<sup>2</sup> welcomed these measures as signs of growing relaxation in the Soviet economy and of a trend towards more freedom for agricultural producers. Mr Khrushchev, it was thought, like Stolypin before him, was 'betting on the strong' by permitting the essential mechanical aids to production to pass into the hands of the 45,000-odd collective farms; but this time, of course, in a setting of overall governmental control and not of unfettered free enterprise.

#### THE 1962 REFORMS: OFFICIAL

#### ACKNOWLEDGEMENT OF SHORTCOMINGS

But once again, in an abrupt change in direction of government policy so characteristic of Soviet develop-

<sup>1</sup> As recently as January 1962 the planners were rebuked for 'bureaucratic interference' in agricultural production methods. They should confine their efforts to procurement, they were told, the quantity and kind of products the farms were to supply to the state. Editorial, 'Basic Questions of the Development of Agriculture', in *Kommunist*, No. 1, January 1962.

<sup>2</sup> For example, Philip E. Moseley, 'Khrushchev's new economic gambit', *Foreign Affairs*, July 1958; Oleg Hoeffding, 'Substance and shadow in the Soviet seven-year plan', *ibid.*, April 1959.

ment, the picture was radically altered by decisions taken at the Plenary Session of the Central Committee of the Communist Party held early in March, 1962. While denying that there was any crisis in Soviet agriculture, and pouring scorn on Western press commentators who had hoped that the Central Committee would decide to 'renounce socialist methods in our agricultural system', Mr Khrushchev laid bare agricultural shortcomings in terms even stronger than he had been using in his public utterances for years past. The Party and the people were 'seriously disturbed' at the state of affairs in agriculture, where the pace of development was not only lagging behind industry but also behind the growth of demand. The population had grown by 29 million since 1953, practically all in urban areas. Real incomes had increased substantially over the same period, but agriculture was not meeting the resulting increased demands for foodstuffs. In 1961 grain production was 16 million tons short of the planned targets, meat 3 million tons, and milk 16 million tons. As a result there had been shortages of meat and butter in some parts of the country. It had taken 40 years, he said, to attain the present levels of output, but now they would have to be doubled and trebled in just a few years.

'If we do not fulfil these tasks, the country will face great difficulties, and serious harm will be inflicted on the cause of building communism. The whole economy can be undermined if the lagging behind of agriculture is not given attention and overcome in time.'<sup>1</sup>

<sup>1</sup> Report by N. S. Khrushchev, 'The present stage of communist construction and the tasks of the Party in improving the management of agriculture', *Izvestia*, 6 March, 1962.

### CHANGE IN FARMING METHODS

Mr Khrushchev followed this forceful exposition of the problem with an equally forceful and specific statement of what was to be done to solve it. The first remedy was a fundamental change in Soviet farming methods with a view to replacing the extensive grass-land system of cultivation associated with the name of the scientist V. R. Williams<sup>1</sup> who introduced it in the 'twenties and 'thirties, by an intensive system of inter-cropping with fodder crops, maize, sugar beet, legumes. The old system had found favour with Stalin, declared Mr Khrushchev, simply because it did not make demands for capital investments for the production of chemical fertilisers and agricultural machinery. These were to be produced in sharply increased quantities, to enable valuable crops to be grown on the land, amounting to about a third of all Russia's arable land, now being under-used in ley farming. The change-over would also involve a fundamental reorganisation of scientific thinking and of teaching methods, and he demanded that the scientists undertake this task.<sup>2</sup>

Over and over again Mr Khrushchev emphasised the simple formula: 'If there is more fodder – there will be more livestock – there will be more meat and milk'. Scientists could make the exact calculations necessary for the success of flights to outer space. They could and they must apply the same techniques to ensure larger supplies of fodder.

<sup>1</sup> A Russian of Welsh extraction.

<sup>2</sup> It was reported in the *New York Times* on 21 January, 1962, that the examining board of a Kazakhstan veterinary college had been reprimanded for approving a dissertation which supported the grassland rotation system. The dissertation was withdrawn.

## FERTILISERS AND MACHINERY

There was plenty of leeway to make up in the production of fertilisers and agricultural machinery. The rate of production of the former was reported to be running at only about one-third of the levels laid down in the current seven-year plan. Only one-quarter of the cows were being milked mechanically, even on state farms; most maize for silage, and sugar beet and potatoes, had to be harvested by hand; there were far too few machines for loading and unloading. The supply to agriculture of some makes of combines and tractors was lower than in 1957, and a factory at Zaporozhe had been allowed to change over to the production of small cars from its previous production of combine harvesters. 'Of course the country could still get along without these cars', said Mr Khrushchev. The scarcity of spare parts for agricultural machinery and their high price was another problem, as was the arbitrary fixing of prices for agricultural machinery.

But while conceding the need to build new factories and expand existing ones to attain the goal of doubling the supply of agricultural equipment, he was most emphatic on the need to train people to use properly the machinery already at their disposal: at present there was a 'barbaric attitude' towards technical matters on some farms, and at harvest time combines sometimes stood idle for more hours than they worked because of inadequate repairs.<sup>1</sup>

<sup>1</sup> A decree published in January 1962 imposed penalties ranging from one to three years imprisonment for careless use of farm machinery resulting in damage or breakage. *Gazette of the Supreme Soviet of the USSR*, No. 1 (1088), 5 January, 1962.

**REORGANISATION OF FARM MANAGEMENT**

The second remedy was reorganisation from top to bottom of the system of management in agriculture, reminiscent of the administrative shake-up in industry in 1957. Regional production boards were to be set up embracing both collective and state farms. At the bottom of the pyramid, the size of the area under one of the new boards would vary with climatic conditions, the nature of the soil, and other factors, but in the debate following Mr Khrushchev's speech it became evident that the general intention was to unite five to 10 raions (districts) under each production board, with 50 to 100 farms under its direction. Each board would have inspectors or organisers, one to every five to seven farms, whose duty would be to maintain a detailed day-to-day check on the fulfilment by the farms of the plans laid down for them by the state, and to make comments or recommendations on the farming methods employed. If any difference of opinion arose between the farm managers and the inspectors, it was to be settled in favour of the former, but if the inspector thought the managers were adopting an 'incorrect attitude', he could report the matter to his production board. The inspectors were to be paid a bonus depending on the success of their farms in fulfilling the plan. The new production boards would be made up of agricultural experts, farm managers, Party officials, and they would work in concert with new committees for agriculture to be set up at all levels. The key official in the boards would be the Party organiser, and at republican and provincial levels the first secretary of the Party would be in direct charge of agriculture. The effect would be to create a chain of

command reaching right back to Moscow, where there would be a high-powered All-Union Committee for Agriculture, headed by a deputy chairman of the Council of Ministers, and including among its members the Minister of Agriculture, the Minister of Procurement, the chairmen of the agricultural committees of the Central Committee of the Communist Party and of Gosplan.

Mr Khrushchev has clamped down these tight planning controls on the farmers little more than a year after he claimed that the collective farms had proved to be successful 'schools of communism' for the peasants, who were no longer reactionary individualists threatening to 'turn back the wheel of progress' as they had been at the start of the revolution, but who had shed their centuries-old private-property habits and were now actively building a new kind of life alongside the urban workers.<sup>1</sup> In his frequent journeyings round the countryside he has evidently found that, with the removal of the control exercised by officials of the machine-tractor stations, the collective farmers lost interest in state plans, and planted what suited their local convenience, or what was dictated by habit and tradition, or the desire for gain.<sup>2</sup> This had brought about the dangerous 'drift' ('samotyek') in agricultural manage-

<sup>1</sup> N. S. Khrushchev at Plenary Session of the Central Committee of the Communist Party, 'Improving the well-being of the people, and tasks of further increasing the output of agricultural products', *Izvestia*, 21 January, 1961.

<sup>2</sup> On 14 January, 1962, *Pravda* printed an article, 'Not from the land, but from the bazaar', by F. Breus, criticising a collective farm near Alma-Ata (Kazakhstan) which neglected the production of foodstuffs in favour of wine-making, out of which it made high profits for the collective farmers and for the 'tolkach' who directed its trading operations.

ment to which he made frequent reference and what he condemned as irresponsibility and the neglect of state interests throughout the whole of agriculture. He was evidently deeply disturbed that no one really knew what was happening on individual farms. As in industry, 'simulation' ('ochkovtiratelstvo') was widely practised to cover up shortcomings in production and as long as the plan for the area as a whole was fulfilled no one bothered to enquire too closely into the reasons for deficiencies in the performance of separate units. Now this had to be replaced by a really close, practical, day-to-day check on plan fulfilment on the farms, under strong Party control at all levels, with a corresponding reorganisation of all agricultural bodies from the Ministry of Agriculture and Gosplan downwards, so as to concentrate their energies on agricultural production.<sup>1</sup>

#### PRICE INCREASES

It was not until the beginning of June that the government's decision was made known to finance the reforms by increasing purchase prices paid by the state to the farms, with corresponding increases in retail prices to

<sup>1</sup> How this day-to-day control was to be exercised was explained in detail in a Central Committee directive, 'On the reorganisation of management in agriculture', which appeared in *Pravda* on 24 March, 1962. In his speech to the Central Committee of the Communist Party of the RSFSR, Mr Khrushchev mentioned a new class of supervisor - the 'instructors' - who were to work on the farms along with the 'inspector-organisers'. The success of the agricultural reforms will be influenced by the extent to which enough of the right type of these officials is forthcoming. - 'Carry out in an organised way the reconstruction of agricultural management', *Pravda*, 28 March, 1962.

the public.<sup>1</sup> The official announcement revealed a double distortion in the economy. Hitherto government purchase prices had not been covering the costs of production of meat and meat products on the collective farms, thus destroying material incentives for livestock rearing. In turn the state had been incurring heavy losses in selling meat to the public at prices which did not recoup their costs. This was to be rectified immediately by increasing purchase prices by 35 per cent for meat and meat products, and by 10 per cent for butter. The corresponding increases in retail prices were to be 30 per cent and 20 per cent respectively.

It was admitted that, in themselves, the increases were undesirable. They would seriously affect family budgets, and would force lower-paid income groups to reduce their consumption of meat and milk. The much smaller cuts in the prices of sugar and some textiles, as well as the measures to be taken to increase the amount of fish on sale, were inadequate compensation.<sup>2</sup> But the increases were unavoidable. Alternatives were examined and dismissed. The necessary funds could not be found by reducing agricultural wages, for this would diminish incentives in the countryside still further. The international situation was such that funds could not safely be diverted from defence: neither could they be with-

<sup>1</sup> 'Appeal by the Central Committee of the Communist Party and the Council of Ministers of the USSR to all workers, farmers, members of the intelligentsia, the whole Soviet people', *Pravda*, 1 June, 1962.

<sup>2</sup> In *Pravda* on 5 and 11 June, 1962, measures were outlined to improve the management and organisation of the fishing industry, and achieve a 20 per cent increase in the supply of fish by 1965: 'On measures to increase the fish catch and the production of the fishing industry'; 'Urgent tasks of the fishing industry'.

drawn from heavy industry without undermining the entire economy. Further increases in the prices of vodka and tobacco would merely encourage 'speculation' which was already active there, as it was in the sale of meat.

It was emphasised that the price increases were 'temporary', but it was also made clear that they would not be lowered until more mechanisation in agriculture, larger supplies of fodder crops, higher productivity of labour in livestock rearing, yielded increased supplies of the products at present in short supply.<sup>1</sup>

#### PRIVATE FARMING

Mr Khrushchev's alarm at the 'drift' in agriculture is not surprising to anyone who has followed the frequent reports in the press showing that the private-property instincts of the peasants are still very much alive. The size of the private plots which the collective farmers were allowed to work varied in different parts of the country, but on the average they were not to exceed one quarter to one half of a hectare. Violations of this rule were, however, extremely numerous. All over the country, from the Baltic States to the Central Asian

<sup>1</sup> This was underlined in a special appeal to agricultural workers published in *Pravda*, 16 June, 1962: 'Appeal by the Central Committee of the Communist Party and the Council of Ministers of the USSR to collective farmers, farm managers and administrators, agricultural specialists, Party and Komsomol members and organisations, to all agricultural workers'. It was emphasised that increased purchase prices would not automatically solve the problem of scarcities, as some agricultural workers seemed to think. On some farms the expenditure of labour and fodder on meat production was so high that even the new prices would not cover them. The farms would have to draw up concrete plans for new buildings, increased mechanisation, above all for larger supplies of cheap fodder.

Republics, came stories of individuals and small groups being able, with the connivance of collective farm managements and local Party officials, to secure plots of land far in excess of the official average, and to use this land for private gain. Thus one man was able to plant six hectares of melons, another raised onions and potatoes on 17 hectares.<sup>1</sup> In still another case, a man made an enormous annual income out of a hectare of land on which he grew produce from hot-houses and forcing-beds.<sup>2</sup>

Even more frequent were complaints of people putting far more energy and interest into working their private plots than into their collective farm. Cases were cited from the Kiev area where men harvested two crops in the year from their personal plots and had 'no time' to work on their collective farms. While they devoted themselves to private farming, the able-bodied members of their families took city jobs, leaving only some relative, perhaps an elderly mother, to 'work' on the kolkhoz. On a state farm in Kazakhstan, communal livestock died in their thousands during the winter for lack of fodder. Privately-owned animals survived, partly because of the personal care lavished on them, partly because they enjoyed fodder hauled out to private farmsteads from state farm stocks.<sup>3</sup>

<sup>1</sup> Editorial, 'Strictly protect collective farm property', in *Socialist Legality* ('Sotsialisticheskoye Zakonnost'), No. 11, November 1960. The cases cited occurred on the 'Kuibyshev' collective farm in the Dzhambul raion (Kazakhstan). Many similar examples were given from other areas.

<sup>2</sup> Editorial, 'He who does not work, neither shall he eat', in *Kommunist*, No. 14, September 1960.

<sup>3</sup> L. Kropachev, 'Private livestock sections on state farm lands', *Kazakhstanskaya Pravda*, 28 January, 1961. Many other instances were given from other districts of the favourable treatment given to private livestock at the expense of state-owned animals on both collective and state farms.

'Independent' market gardeners in a remote part of Leningrad province were making large profits by growing cucumbers and selling them not only in near-by Smolensk but as far afield as Moscow and Archangel.<sup>1</sup> Private entrepreneurs were even active in the sphere of state purchases, that is, the amounts of produce which the collective farms had to deliver to the state at fixed prices. There was an astonishing tale of two brothers, Lev and Yefim Krol, who worked for ten collective farms, and were doing big business in this line, helping the farms to meet their quotas. They used their own lorries, built their own receiving centres for livestock, hired their own staff of assistants, buyers and guards; in fact, said the writer, they acted exactly like a privately-owned company.<sup>2</sup>

#### CONDITIONS IN RURAL AREAS

The poor state of mechanisation on farms and the need for large improvements in living conditions in many areas of rural life were also mentioned frequently in the press. One writer discussed the reluctance of young people to work on the land.<sup>3</sup> He himself was looking after pigs on a collective farm in the Ukraine, but out of 43 students who had finished their secondary education with him in 1958, only five were working in agriculture. The others had taken town jobs selling ice-cream, acting as conductors on buses, working in pensionable office

<sup>1</sup> M. Garin and K. Sevrikov, 'The fate of small towns', *Izvestia*, 28 October, 1960.

<sup>2</sup> A. Kanayev and V. Prokudovich, 'Smart Fellows', *Izvestia*, 18 October, 1960.

<sup>3</sup> 'Why did only five of us stay?', by Leontii Lukashevsky, Leningrad Collective Farm, Kirovgrad Province, in *Komsomolskaya Pravda*, 17 December, 1960.

posts. For this he blamed the long hours, the lack of mechanical aids, the primitive living conditions still characteristic of rural life. It was all very well to supply tractors to the farms – 'the tractor is still king of our fields' – but that was no comfort to him, when he had to work from 5 am until 8 pm, with no appliances to help with heavy jobs such as hauling manure or spreading feed. Another serious drawback was the lack of shopping facilities, of communal amenities such as nursery schools, for this meant that wives could not continue working after marriage. Young people were now given a good education and could not be expected to spend their lives doing hard manual tasks which machines could take over.

Another correspondent gave a depressing picture of life on one of the less prosperous collective farms in Kiev province.<sup>1</sup> He was one of the 30,000 volunteers who had responded to the government's appeal in 1955 to go and help some of these farms to raise their productivity. But after five years as Chairman, he found himself caught in a vicious circle. Because the farm was poor, it found difficulty in paying off outstanding credits: therefore it could not ask for new credits to institute improvements, and so it remained backward, to the government's displeasure and its own discontent. He listed some of the improvements his farm badly needed and could not pay for: new farm buildings; a new road to the neighbouring town; good pedigree stock; more mineral fertilisers and high-quality seed;

<sup>1</sup> 'What a collective farm chairman finds disturbing', *Selskaya Zhizn*, 13 December, 1960. Letter to Mr Khrushchev from S. Davidyuk, Chairman of the 'Lenin' collective farm in the village of Sulimovka, Kiev Province, quoted in the *Current Digest of the Soviet Press*, 11 January, 1961.

a bulldozer and a repair shop; well-qualified staff, book-keepers, economists, planners, agronomists, secretaries; skilled building workers; agricultural machinery and spare parts. Mr Khrushchev's insistence on the need to inquire into the working of each individual farm included the aim of raising the efficiency of the 'lagging' collective farms. This may in time bring some relief to cases such as the one outlined above, particularly as collective farms have been told to establish special funds out of which such farms can be helped. But it is not likely that results will be achieved quickly.

There may be no crisis in Soviet agriculture, but there is certainly a widespread malaise of long standing, which may have its roots in the gap between rural and urban standards of living. Since collectivisation, the peasants have not only carried a disproportionate share of the sacrifices imposed by industrialisation but have also been forced by their system of remuneration – payment in kind, at irregular intervals, for 'labour-days' performed – to carry the risks of harvest variations as well. They are essentially residual claimants, getting what is left after the government has taken its share and the collective farms have ploughed back as much as they want into their 'undistributed funds'. In his speech to the Central Committee Mr Khrushchev admitted that agriculture had been undermined by the government's practice under Stalin of buying agricultural produce at prices that failed to cover costs of production, and rebuked some collective farms for holding back too much in 'undistributed funds' to provide schools, hospitals and so on, at the cost of giving too little to their members in 'labour-day' payments.

Rewards for the same kind of work vary widely from one collective farm to another, and the general level of remuneration is well below that of industrial workers. In addition to suffering from a lack of the communal amenities which ease life in the towns, it is not generally realised that the peasants, who still form half the population, do not share in social insurance benefits. They have no legal claim to sickness benefits, retirement pensions, paid holidays, and get only what their collective farm may be able to afford out of funds accumulated for these purposes.

#### PROSPECTS FOR THE FUTURE

The present reforms hold out little hope of any immediate amelioration for the 'infantry' of Soviet agriculture of this relatively inferior position. Although Mr Khrushchev vigorously defended the general principle of material self-interest in agricultural work, he had nothing specific to say on how it was to be secured for the rank-and-file workers. Out of more than 50 speeches recorded in the subsequent debate, only three mentioned material incentives; in one the reference was confined to bonuses to tractor-drivers and mechanics,<sup>1</sup> another mentioned a premium system on state farms,<sup>2</sup> and only one gave specific figures showing the amount of produce actually paid out in incentive payments.<sup>3</sup> The trade union speaker stated flatly that very little had been done on the farms to introduce such pay-

<sup>1</sup> Speech by F. A. Tabayev, First Secretary of the Tatar Provincial Party Committee, *Izvestia*, 9 March, 1962.

<sup>2</sup> Speech by A. V. Basov, First Secretary of the Rostov Provincial Party Committee, *ibid.*

<sup>3</sup> Speech by I. I. Bodyul, First Secretary of the Moldavian Party Committee, *Izvestia*, 8 March, 1962.

ments, and that this failure had had an adverse effect on agricultural production, as had the acute shortage of housing in some areas, the lack of canteens, and the poor medical services. Last year, he said, as many doctors had left rural areas as had come into them, leaving many rural medical institutions without qualified doctors.<sup>1</sup> He urged a complete overhaul of the agricultural wages system and the establishment of labour and wages departments in every one of the new production boards, as well as the appointment of a rate-setting specialist on every large farm.

One positive result of the application of Mr Khrushchev's 'new look' is that agriculture can no longer be treated as the Cinderella of the Soviet economy.<sup>2</sup> Events have forced the Soviet leadership to realise that they cannot continue to limp along with a highly developed industry alongside a persistently backward agricultural system. To redress the unbalance, they are relying on the tried and tested methods of sweeping administrative reform, intensified Party control, exhortations to members of the Communist Party and to young people to go and help on the land, an emotional identification of the new methods with the general cause of communism, all the familiar features of the Soviet 'campaign' method of securing economic improvement. If the method works, and if, in addition, agriculture gets the fertilisers, the machinery, spare parts, insecticides and other forms of material help which have been promised, some of the benefits result-

<sup>1</sup> Speech by V. V. Grishin, Chairman of the Central Union of Trade Unions, *Izvestia*, 10 March, 1962.

<sup>2</sup> Mr Khrushchev's concluding speech, 'The Soviet people will fulfil the programme for the furthest development of agriculture', *Izvestia*, 11 March, 1962.

ing from increased production will in time trickle through to the general body of agricultural workers. For the present, they still stand at the end of a long queue, and they will still have to bear the brunt of any failures or shortcomings in carrying out the new scheme. Moreover, the transference to a more intensive system of land cultivation will cut down the amount of pasture available for their privately-owned livestock, and they will have to put up with a much greater degree of bureaucratic control over their activities. Until the existing inequities between town and country are corrected in fact and not only in words, it is a fair presumption that the peasants will continue their endeavours to satisfy their own desires, even within the abruptly narrowed limits of the collective system.

## 5. HOUSING

### THE PRIVATE SECTOR

As in agriculture, there is a large private sector in housing. To begin with, collective farm dwellings, housing half the population, are almost entirely privately built and owned, and consist mostly of one-storey structures, typically without plumbing and other services.<sup>1</sup> In urban areas, individually owned houses account for over one-third of the total housing fund.<sup>2</sup> As the rents of government-built flats are very low, usually about 5 per cent of income, and official policy aims at providing every family with a well-appointed flat at no cost at all in twenty years' time, only a very compelling reason could persuade so many people to go to the trouble and expense of building their own dwellings.

The reason is the acute shortage of housing, arising from the physical destruction in two world wars, severely intensified by neglect during the years of concentration on industrial progress. It is only now

<sup>1</sup> 'Do we need houses like this?', by K. Ivanov, A. Peremyslov and A. Ryabushin of the Institute of Architecture and Building, in *Izvestia*, 6 July, 1961.

<sup>2</sup> 'On the right of personal ownership in housing', *Soviet Government and Law* ('Sovietskoye Gosudarstvo i Pravo'), No. 7, July 1961.

that substantial efforts are being made to improve the situation, and in carrying out their policy the government has faced many complexities, both in the private and in the state-controlled sectors.

It is officially admitted that the housing problem remains acute, and that the help of private enterprise is still essential. True, the government stopped credits to private house builders in 1959, but in this they may have been actuated as much by the shortage of building materials, and the need to conserve them for the official programme, as by their dislike of an activity which encourages the 'private property' mentality among their citizens.<sup>1</sup> They also cannot overlook that housing remains the only outlet for private investment, apart from the savings banks, and to curb it still more would merely accentuate housing difficulties and increase inflationary pressures throughout the economy.

While tolerating private house-building for the present, official policy does all it can to keep it within acceptable ideological limits. There is much discussion about the nature of personal property in housing under communism, and the official line is that it can be of a consumer nature only. It must not on any account be used as a source of unearned income.<sup>2</sup>

#### VIOLATIONS OF OFFICIAL POLICY

This injunction is widely disregarded in everyday life. A collective farm in the Moscow area sold ten hectares

<sup>1</sup> *The World Today*, Royal Institute of International Affairs, November 1960, p. 461.

<sup>2</sup> 'For all, in the interests of each', *Izvestia*, 30 August, 1961. Academician S. G. Strumilin answers questions from readers about personal property under communism.

of its land for building 'dachas' (country houses) for a group of writers. The proceeds, over half a million roubles, were disguised in the farm's accounts as funds allotted to the construction of a rural club.<sup>1</sup> A good deal of private building was co-operative in character, the members of the housing association contributing their money and labour and retaining the right of private ownership in one of the flats. Cases were cited from Tbilisi (Georgia) of people who already had housing accommodation joining these associations and renting out the additional space thus acquired. A man employed as a contractor in one such co-operative even used two of his own cranes on the job.<sup>2</sup> A case which caused a furore was reported from Kuibyshev, on the Volga, in 1960.<sup>3</sup> It concerned a housing association originally formed by a group of scientists, doctors and engineers to build dachas for their members in a picturesque undeveloped area outside the city. As time went on, these scholarly members of the Kuibyshev Industrial Institute were replaced by more commercially-minded men, who cultivated the large gardens of the dachas with hired labour and disposed of the produce

<sup>1</sup> *Sotsialisticheskoye Zakonnost*, No. 11, 1960. The Executive Committee of the Moscow Provincial Council of Deputies was censured by the writer for failing to prevent this action of the 'October Revolution' collective farm in the Zvenigorod raion, and even sanctioning it. Half a million roubles is about £200,000 at the current rate of two and a half roubles to the pound sterling. A decree of the Supreme Soviet revalued the rouble on 1 January, 1961, making ten roubles of the old money worth one of the new: *Gazette of the Supreme Soviet of the USSR*, No. 18 (1002), No. 136, 12 May, 1960.

<sup>2</sup> *Kommunist*, No. 14, 1960, *op. cit.*

<sup>3</sup> Yu. Oklyanski, 'The Case of the Cold Ravine', *Literaturnaya Gazeta*, 20 December, 1960 and 14 March, 1961.

in the town markets at high prices. Two aspects of this case came under special condemnation. One was that the men responsible had used their official positions to obtain state materials and labour for building additional dachas, even utilising the services of young apprentices from the local state labour reserve school. The other was the shortcomings of the law which allowed these private enterprise activities to continue, although they had been publicly known for more than five years.

The law as it stood, and court practice arising out of it, left so many loopholes that it was difficult to eradicate what were officially considered malpractices. There was no certainty whether the right of private ownership in a dwelling extended to each member of a family or only to the family as a whole. There was no firm ruling that ownership of a house or flat disqualifies an individual from joining a co-operative association and acquiring another dwelling. The right to build 'auxiliary residential and service structures' was intended to apply only to summer kitchens, barns, and similar buildings for the owner's use, but in practice frequently served as an excuse for erecting several houses on a plot meant for only one, providing the owner with a source of unearned income, of which many did not hesitate to avail themselves.

#### TREATMENT OF IRREGULARITIES

Even members of the Communist Party could become implicated. From Uzbekistan came reports of inconsistent treatment meted out to Party members who took advantage of their official positions to obtain

scarce materials and build houses for themselves. In one case the offenders were publicly named, dismissed from their posts, and had their houses confiscated; in another they got off with a reprimand.<sup>1</sup> The same publication devoted a whole article to the case of Zikeyev, responsible head of a department in a state farm, who applied for a plot on which to build a dacha, when his farm set aside some land for this purpose. He was devoted to his small grandson, and wanted to build a separate home into which his son and daughter-in-law could move with the child, giving the young people a chance to live in healthier surroundings than could be obtained in the three-roomed flat where they were all living together.<sup>2</sup> But it was one thing to get a permit to build, quite another to get the work done. The only people available to dig the foundations were 'free workers', a group of anonymous monopolists, who demanded an exorbitant price which Zikeyev had no alternative but to pay. His permit stipulated that the dacha must be completed within three years, and if he let these workers go, he might lose at least a year. Troubles multiplied at every stage of construction. To get the necessary building materials he had to resort to 'blat' and use his personal influence with a fellow director of the state farm, even with the manager of a factory under his own jurisdiction. He could not get timber at all, except from 'private operators' at very high prices. Roofing tiles were unobtainable, until he and his fellow dacha-builders on the farm got together,

<sup>1</sup> Editorial, 'He who does not work, neither shall he eat', in *Party Life* ('Partiinaya Zhizn'), No. 19, October 1960.

<sup>2</sup> G. Yelizavetin, 'What is happening to Zikeyev?', *Party Life*, *op. cit.*

turned one of their members into a 'tolkach', sent him off on an 'official' visit to a town where he managed to secure supplies for them all 'on the side'. By this time expenses had mounted alarmingly, and to recoup at least a proportion of them, Zikeyev, after assurances from his wife that 'everybody was renting', let part of the dacha for a short time.

The whole set of transactions came to light when his daughter-in-law, a member of the Communist Youth Organisation (Komsomol) denounced him to the local Party secretary, and the morality of dual private ownership of housing, the right to let, and so on, were thrashed out at a Party meeting. The unfortunate Zikeyev, his health seriously affected by worry, and threatened with expulsion from the Party, felt that he had no option but to hand over the ill-starred dacha to his farm.

#### TYPES OF BUILDING

Official policy strongly favours multi-storey blocks of flats, preferably five-storey structures, without lifts, and with open spaces and other amenities provided on a communal basis. Low-density urban housing is condemned as wasteful of valuable space, leading to the isolation of families, making it more difficult to provide the services which relieve women of household duties and free them for work in 'social production', and turning citizens away from the ideals of communal living. But even state housing plans continue to make substantial provision – 20 to 25 per cent of the whole – for one- or two-storey structures with access to private gardens, and much of private construction is of the

same kind. The acute shortage of architects (the schools were turning out only 540 per annum, it was said, although 25,000 per annum were needed), and the absence of planning in many cities, make it difficult for the government to exercise control.<sup>1</sup> In country districts, the absence of standard designs for houses, cultural and service buildings and warehouses, was also felt to be a great disadvantage. For dwelling-houses, the two- or three-storey building, with flats on two levels, was thought to be the most economical, although Mr Khrushchev recently advised collective farmers to build multi-storey blocks instead of individual houses.<sup>2</sup> But the lack of a properly organised supply of building materials made it difficult to plan at all, and made recourse to the open market unavoidable. There was a report of 200 collective farms in the Krasnodar territory spending 14 million roubles in this way in the course of two years.<sup>3</sup>

#### THE OUTLOOK

The government's housing plans aim at abolishing sub-standard housing and overcrowding in ten years, and achieving the 'norm' of one person to a room in 20 years. 'Only when man draws abundantly from the "ours" will he gladly give up the "mine"', said an authority recently.<sup>4</sup> Even the full achievement of these

<sup>1</sup> 'Construction and the task of the architect', a speech by A. V. Vlasov at the Third All-Union Conference of Soviet Architects, *Pravda*, 19 May, 1961.

<sup>2</sup> *Izvestia*, 6 July, 1961, *op. cit.*

<sup>3</sup> Jan S. Prybyla, 'Private Enterprise in the Soviet Union', *The South African Journal of Economics*, Vol. 29, No. 3, September 1961. 14 million roubles is about £5½ million. See footnote 1 on p. 53.

<sup>4</sup> S. G. Strumilin, *op. cit.*

aims will not spell 'abundance' in all parts of the USSR by any reasonable standard, and so the indefinite continuance may be expected of private building, a lively free market in building materials, the activities of private contractors, and the letting and sub-letting of rooms and houses.

## 6. LABOUR

### THE OFFICIAL SECTOR

Russia has come a long way since the days of the first five-year plan (1928-32), which saw the beginning of the tremendous influx of new recruits, mainly unlettered peasants and women, into the ranks of industrial labour. By 1940, the non-agricultural labour force numbered over 30 million, having increased by approximately 18 million in the short space of 12 years. Now Russia's industrial might is supported by a force of 60 million workers, many of them highly skilled, with new recruits given facilities to improve their qualifications.

Theoretically the labour field offers little scope for the operation of market influences. Wages and salaries are controlled by the central government through the planning system, there are no independent trade unions in the Western sense, and no employment exchanges or any nation-wide system of advertising vacancies. Moreover severe governmental controls have been imposed on industrial workers throughout the plans in order to improve standards of labour discipline and lower high rates of labour turnover. Dismissal, with possible loss of housing accommodation, manipulation of social insurance benefits to favour the long-service worker, the issue of internal passports and labour books

without which workers could not be taken on in new jobs, were some of the means used before the war.<sup>1</sup> During the war these were reinforced by universal labour conscription, and labour only became fully mobile again in 1956.

In spite of all this, market influences have remained active in this sector of the economy.<sup>2</sup> In the periods when controls were used, they were constantly eroded by the scarcity of labour relative to the ambitious plan targets, and by the elaborate system of piece-rates and bonus systems which gave management room to manoeuvre in their desperate search for workers, by manipulating officially determined norms and grades. With the removal of controls and the continuance of high planning targets, this process has continued.

Government control is more effective in the case of white-collar workers, teachers, doctors, civil servants and the like, whose position has accordingly suffered a relative decline *vis-à-vis* industrial workers. Periodically the government undertakes an overhaul of wages and salaries, to correct anomalies and ensure a more accurate correlation between rewards and skills. But this process is slow – the last one began in 1957 and was due to be completed in 1961 – and cannot hope to keep pace with the constantly changing pattern of supply and demand relationships in the labour market.

The government still exercises 'control by exhortation' over the 8 million members of the Communist Party and the 18 or 19 million Komsomol members, who are

<sup>1</sup> Margaret Miller, *Labour in the USSR*, British Association for Labour Legislation, London, 1942; G. R. Barker, *Incentives and Labour Productivity in Soviet Industry*, Basil Blackwell, Oxford, 1956.

<sup>2</sup> Alec Nove, *op. cit.*, p. 115 *et seq.*, and p. 231 *et seq.*

in theory bound to go and work wherever the Party sends them. This has been very effective in the past, and the Komsomol members have contributed youthful energy and enthusiasm to pioneering projects in distant parts of the country, the far North and Siberia. Before the war, the machine-building, ship-building and metallurgical town of Komsomolsk-on-the-Amur was built entirely by their labour, in conditions of great hardship.<sup>1</sup> But the revolutionary ardour of the 'twenties and 'thirties has been diluted by the three- to four-fold increase in the membership of these organisations, and by the increased material prosperity of the 'fifties and 'sixties.<sup>2</sup> In making the customary appeal to youth in his speech introducing the agricultural reforms of March 1962, Mr Khrushchev warned against the 'professional volunteers' who responded readily to such calls, worked for a few weeks, and then returned to the comforts of home.

The economic evolution within the Soviet Union has brought about many changes in the attitude towards inequalities of income. In the idealistic early days of the Revolution, the incomes of high-ranking employees, including members of the government, were closely controlled, and the spread of wages between the highest and lowest paid workers throughout the country was kept as low as 2 to 1. Under the pressures of mounting inflation and the need for higher productivity, the spread increased to 8 to 1 for industrial workers before

<sup>1</sup> Nicholas Mikhalov, *Land of the Soviets*, Lee Furman Inc., New York, 1939, p. 201; G. D. B. Gray, *Soviet Land*, Adam and Charles Black, London, 1947, p. 225; Harry Schwartz, *op. cit.*, pp. 33, 226.

<sup>2</sup> Alexander Werth, *The Scotsman*, 18 and 19 May, 1962.

the end of the New Economic Policy,<sup>1</sup> a tendency enhanced by Stalin's attack in 1931 on 'levelling' ('uravnilovka') in remuneration. The Stakhanovite campaign, launched in 1935, increased wage differentials still further by encouraging large rewards to the relatively small number of exceptionally productive industrial workers.<sup>2</sup> After the war, adjustments in favour of the lowest paid industrial workers reduced differentials somewhat, but in the early 1950s they were still commonly as high as 15 to 1.<sup>3</sup> Since 1959 the official trend has been towards improving the wages of workers in the lowest and medium scales, with the ultimate aim of returning to differentials of not more than 2 to 1 for industrial labour.<sup>4</sup>

It is harder to evaluate the real rewards of salary-earners because of the hidden emoluments of office. But it may be surmised that differentials between the highest and lowest paid workers in the country as a whole will continue to depart widely from the ideals of 40 years ago, probably remaining at 5-10 to 1 or even higher.

#### THE 'FREE' WORKERS: PRIVATE ENTERPRISE ACTIVITIES

Outside the official sector there is a considerable volume of economic transactions of which there are no formal records, and which cannot, therefore, be

<sup>1</sup> Margaret Dewar, *Labour Policy in the USSR*, Oxford University Press for the Royal Institute of International Affairs, 1956, p. 134.

<sup>2</sup> Alec Nove, *op. cit.*, p. 121.

<sup>3</sup> Harry Schwartz, *op. cit.*, pp. 463-468.

<sup>4</sup> B. Sukharevski, 'The working day and wages', *Kommunist*, No. 3, February 1960.

evaluated in specific terms. Their importance is attested by the constant stream of disapproving attention they attract from official sources, and by numerous references in the press. These private enterprise activities range over a wide field, from large-scale building operations involving the use of expensive equipment, to the man or woman in a state job who does spare-time repair work or dressmaking.

In the town of Gomel, in the west of Russia, one Dolbeshkin was said to have made himself indispensable over a wide area as a building contractor, serving government co-operative associations and local industry committees. In two years he had been responsible for putting up seven new factories, and carrying out capital repairs in five existing factories. The committees of local industry had to approve supplementary estimates to cover their expenditure on his services. He hired labour, specifying their qualifications and wages on his own authority. At Mogilev, about 50 miles away, another man, Aladyev, was making large profits by building electricity sub-stations, putting up high-voltage overhead lines and bringing electricity to farms and local hospitals.<sup>1</sup>

Loading timber was a favourite occupation of gangs of men who disliked regular occupation in a state establishment, preferring to hire themselves out to collective farms on an independent basis. The existence of a large band of seventy of these individualists was reported from the village of Yefimov in Leningrad province. They determinedly preserved their free-lance mode of life by producing medical certificates, refusing jobs offered to them on the grounds that they were

<sup>1</sup> *Izvestia*, 18 October, 1960, *op. cit.*

'unsuitable', insufficiently paid, and so on.<sup>1</sup> Collective farms in Saratov province were reproached for hiring similar bands of 'private operators', not only for handling timber, but for constructing farm buildings.<sup>2</sup>

Three cases of large-scale private enterprise were brought to light in Rostov.<sup>3</sup> In the first, a man named Damaskin had a private factory, a large two-storey building with a glass roof, from which he conducted a lucrative trade in tropical fish. His spacious yard was full of railway wagons carrying cement, iron, timber. A second, Burigin, bought young rabbits on the free market, reared them, and sold them to collective farms, schools, institutes, zoological gardens. His wife supplemented the handsome family income by selling rabbit meat on the market all the year round. In the third case, a group of beekeepers conducted their business on the lines of a private company. They bought up enormous quantities of sugar in the shops to feed their bees, sold their honey at 'fabulous' prices which enabled them to build their own houses, run cars, and live in princely style. Taking advantage of some loophole in the law, all these operators succeeded in avoiding any form of taxation.

Personal observation, and evidence in the press, bear witness to the existence of a numerous class of artisans and small craftsmen, dressmakers, television, radio and shoe repairers, makers of sledges, pitchforks, household crockery, dealers in such varied goods as jazz records, church bells, wedding crowns, paintings,

<sup>1</sup> N. Petunin, 'Free workers at Yefimov', *Literaturnaya Gazeta*, 1 November, 1960.

<sup>2</sup> *Kommunist*, No. 14, 1960, *op. cit.*

<sup>3</sup> I. Mikhailov, 'Protected Kings', *Izvestia*, 14 May, 1961.

sculptures, ikons, motor-bicycles, even grave memorials and undertaking services. In the latter case, reported from Odessa, the entrepreneur had his own staff of seven, and his own fleet of cars for funeral processions.<sup>1</sup> At the 21st Congress of the Communist Party in 1959, it was stated that it was no use trying to increase the output of sugar without at the same time controlling home brewing and distilling which used up 'enormous quantities' of sugar, a frank admission of the widespread production of alcoholic drinks.<sup>2</sup> It is impossible to estimate the numbers of such workers, but there is no doubt that they represent a considerable body of economic activity and that they point to continuing shortages of many varieties of consumer goods, as well as to the need among many sections of the population to supplement inadequate incomes.

#### GAPS IN THE PLANNING SYSTEM

Sometimes they flourish because of the incompleteness of the planning system, which is unable to carry its controls into every distant corner of Russia. Where gaps are allowed to appear, private enterprise rushes in to fill them, as it would do in any country. In a remote part of Leningrad province, for example, the state planners' inability to subsidise the development of local industry left private craftsmen without competition. They promptly proceeded to meet the demand for consumer goods in everyday use, wheels, carts,

<sup>1</sup> P. Ilyashenko, 'The Kidnapped Madonna', *Literaturnaya Gazeta*, 20 October, 1960; O. Lavrova and A. Lavrov, 'Repin on the sly', *ibid.*, 4 March, 1961; Editorial in *Partiinaya Zhizn*, No. 19, 1960, *op. cit.*; *Izvestia*, 28 October, 1960, *op. cit.*; *The South African Journal of Economics*, *op. cit.*

<sup>2</sup> Speech by T. S. Maltsev, *Pravda*, 5 February, 1959.

sledges, nails, small agricultural implements, household requisites such as scissors, forks, textiles. Half the population in one town were said to be occupied in this way, and to be doing well out of it, since the average level of deposits in the town savings bank was double the national average.

#### THE ANONYMOUS 'SPECULATORS'

In view of official disapproval, people engaged in these activities usually work in obscurity, except when some enterprising newspaper correspondent turns the spotlight of publicity on them. In the Zikeyev dacha-building case described earlier, the group of four foundation-diggers – nobody knew their names or where they lived – were described as standing by in indifferent silence, ready to walk away if the exorbitant demands of their leader were not met – as hard-boiled a group of 'capitalists' as could be encountered anywhere. More often they are the nameless 'speculators' who supply the goods unobtainable through state channels, only to melt into the background as soon as the transaction is complete, leaving the buyer to carry the responsibility in case of trouble.

This happened with a communist official in Uzbekistan who was dismissed for 'breaking the laws of Soviet trade' in order to buy his young son an expensive motor-cycle from an unknown supplier.<sup>1</sup> A Soviet legal publication criticised this immunity when reporting on the case of an official in a Moscow plant who had been arrested for buying 400 metres of electric wire through illegal channels. It transpired that the official had a clean record and had no personal stake

<sup>1</sup> *Partiinaya Zhizn*, No. 19, 1960, *op. cit.*

in this transaction. He merely wanted to oblige some collective farmers who were pressing him to get electricity brought to their village. He had done his best to get the wire legally, but the state shops had none. Eventually, with some misgivings, he acquired it from a 'speculator', and the lights went up in the village. But the local committee for the protection of state property got wind of the incident, with the result that the official was pilloried while the supplier went free.<sup>1</sup>

Sometimes these private enterprise activities fall into the criminal class. An indignant employee of the Magnitogorsk metallurgical combine wrote to *Izvestia* about two local men, Lakhman and Gemba, who had gone to extreme lengths in defence of their private fruit gardens.<sup>2</sup> The first man's efforts had recoiled upon himself. He had mined his orchard to protect his apples from marauding small boys, but had inadvertently stepped on one of his own mines, as a result of which he lost the sight of an eye and spent months in hospital. In the second incident the owner, going out to investigate a noise in his garden at night, shot without warning and fatally wounded an intruder who was climbing over his fence. This was said to be the

<sup>1</sup> 'The guilt is not established', by A. Aduyev, Peoples' Judge, in *Sovietskaya Yustitsia*, No. 12, 1960. The writer strongly condemned the local legal authorities for taking the extreme step of placing Popov, the official in question, under arrest, and keeping him in prison for three months. This view was upheld by the writer of the Editorial in *Sotsialisticheskoye Zakonost* cited on p. 53, who wanted to know why the local procurator and militia had not uncovered the 'sources of speculation' by finding the unknown seller.

<sup>2</sup> 'Blown up by his own mine': letter from F. Pivovarov with editorial comment by A. Adzhubei, in *Izvestia*, 8 September, 1961.

culmination of a trend among private owners in the district to take increasingly strong measures to defend their property by putting up high walls, keeping savage guard dogs. The correspondent who discussed the activities of the Gomel building contractor also noted that the man's house was surrounded by a very high wall and was more like a fortress than a private dwelling.

But deliberately criminal acts form a small percentage of all this private economic activity, and in quantitative terms the activity itself can only account for a relatively small proportion of state-controlled production, although it must have some effect in distorting state plans for labour, materials and finance.<sup>1</sup> By far the greater part of the entrepreneurs' efforts would seem to be beneficial from the common-sense point of view. Communities far from the centres of production and neglected by government planning organs, set to work with commendable initiative – from our point of view – to supply their own needs. The private entrepreneur, in making profits for himself, shows a willingness to take risks, and puts a lot of energy and initiative into satisfying a strong demand, which would otherwise go unsatisfied, for essential or desirable commodities and

<sup>1</sup> On 9 January, 1962, *Sovietskaya Kirgiziya* reported ('Plunderers and currency speculators are unmasked', by P. Chvertko) the uncovering of a group of 'embezzlers of state property' who had been operating for a long time at a knitwear and weaving factory. Among the people indicted were the Deputy Minister of Trade of the Republic and the Director of the local Regional Economic Council. Their activities had concealed from the planning agencies large quantities of 'extremely scarce' materials, such as viscose fibre and wool, and had lowered the indices of the industrial finance plan. Four of them were subsequently sentenced to death. – 'A deserved punishment', *Izvestia*, 22 July, 1962.

services. Collective farms and local industry would get state building materials and labour at much cheaper rates, if they were available. When they are not, it hardly seems reasonable to blame them for getting the jobs done as best they can.

#### THE IDEOLOGICAL BACKGROUND

It is for ideological rather than purely economic reasons that government spokesmen spend so much time in condemning all such activity in vehement and quite non-selective terms. Every such exhibition of 'private property mentality' is, they maintain, a capitalist trait, a survival from the past, and an impediment to building the communist future. They devote large sections of their public speeches to the emergence of the 'new Soviet man', who will be the mainstay of the country when the transition to full communism is completed in twenty years' time. He will be a highly developed individual who will work, not because he has to, but because some form of socially useful labour will have become a 'first necessity of life' for everyone. By then there will be such an abundance of consumer goods that material self-interest will be completely outmoded, and it will be possible to change the slogan 'From each according to his abilities, to each according to his work' to the more advanced 'From each according to his abilities, to each according to his needs'. Until that time arrives, however, there is to be no over-optimism about moral incentives. In his speech to the Party Congress in the autumn of 1961, and again at the Central Committee in March 1962, Mr Khrushchev

declared that the success of current plans would depend on the preservation of the worker's material interest in the job. 'We must learn to work with people as they are', he said. This being so, we may expect that Soviet man will continue to resemble his capitalist counterpart for as far ahead as can be seen.

In commenting on the incidents at Magnitogorsk, Mr Adzhubei<sup>1</sup> said that the behaviour of the guilty men was contrary to communist morality. While accepting communal benefits such as holidays, educational and health services, they still held on to their individualistic beliefs: 'We have done nothing wrong', 'These apples are mine'. Such 'greedy idlers' would have to be eliminated, and the sooner the better. In similar vein, editors in influential journals deprecate the influence of 'speculators' and 'idlers' in undermining the true socialist attitude to work.

Some recent press references indicate that there is thought to be a danger of government propaganda backfiring. Glowing official descriptions of the abundance of material goods under communism were meant to be a stimulus to hard work, now and in the future after full communism was established. But they seem to have inspired some people with a desire to enjoy such benefits at once, and without necessarily working hard for them. There is criticism of the lack of interest shown in the work of the 'peoples' guards' ('druzhiny'), voluntary organisations which have been formed in many communities to support government policy by helping to preserve public order and holding non-conformers up to

<sup>1</sup> Editor of *Izvestia*, and Mr Khrushchev's son-in-law.

social condemnation.<sup>1</sup> At the same time the fear is expressed that where these organisations are active the local police tend to relax and let their job be done for them.

From all this the general impression emerges that in trying to enforce high ideals of 'socialist labour' in conditions of acute scarcity in many vital sections of consumption, official policy is swimming against a current of popular feeling that is too strong for it, and that will continue to result in the diversion of materials and labour into the private enterprise sector so long as shortages continue - which means for at least many years to come.

<sup>1</sup> A recent decree increased the penalties for attacks on members of the militia and of the peoples' guards, ranging from 15 days' imprisonment for refusing to obey their orders to the imposition of the death penalty for grave cases of attacks on these officers by 'criminals and other anti-social elements': *Gazette of the Supreme Soviet of the USSR*, No. 8 (1095), 21 February, 1962.

## 7. CONCLUSION

Market influences in the USSR, although relegated in theory to the limbo of the capitalist past, remain remarkably lively, not only in the sectors of the economy recognised as free, but in the official sectors as well. They are of decisive importance in marketing foodstuffs and significant in the provision of housing, they affect the flow of labour to industrial projects, modify plan performance, and flourish in a multitude of fringe activities outside the official plan.

In the absence of reliable statistics it is only possible to guess at their relative significance in the economic life of the country. Given the chronic difficulties of supply and the continuance of ambitious plan targets, it might be assumed that anything up to one-quarter of the necessary supplies reach industry through non-official channels. If private craftsmen, artisans and dealers limited themselves to strictly legal transactions, refraining from employing assistants and selling only goods produced by their own labour at prices approximating to those charged by state organisations for similar goods, their output would amount to an insignificant proportion of national economic activity, probably one per cent or less. But there is abundant evidence that their

operations extend far beyond these limits, and that they play a perceptible role in supplying commodities and services for which the state plan makes insufficient provision or none at all. In agriculture, not only do people still rely on the private sector for about half the foodstuffs they consume, but the farms depend on free enterprise for some of their labour needs in harvesting, timber handling and building construction – possibly as much as 10 per cent or more of their requirements in this sphere. Remembering the extent of private house-building and ownership in rural areas, the importance of the private sector is biggest of all in housing, where it supplies something in the region of two-thirds of present needs. Looking at all this, and taking a conservative view, it would be by no means unreasonable to estimate that something like one-fourth of all forms of economic activity in the USSR is in private hands, or moves through non-official channels.

None of this is in accordance with official doctrine, which from the earliest days of the Revolution has aimed at building a society in which the desire for the common good will replace the drive for personal gain. However, the pressure of events has from time to time forced the government to adopt an ambivalent attitude towards free enterprise. They disapprove of it, but they are willing to make use of it for their own ends. When economic difficulties became overwhelming at the end of the period of war communism, the government released private enterprise in order to get the economy on its feet again. But this was merely a case of 'reculer pour mieux sauter': as soon as the economy was restored, private manufacturing and trading were eliminated and government controls re-imposed. In

the same way, during the period of intensive industrialisation before the war, and the period of reconstruction following it, official policy gave every encouragement to the building of houses and flats by private individuals, and by state concerns for their workers. As soon as industry was restored to a satisfactory level, an official campaign against private house-building and ownership was initiated. Foreign observers who have studied the situation are unanimous that a great deal of what is really private initiative is tolerated in industry, as long as it serves the ends of plan fulfilment; and authoritative Soviet speakers underline the need to preserve material self-interest with at least as much enthusiasm as they dedicate to the development of the 'new Soviet man' for whom this very incentive will be meaningless.

The elimination of private enterprise remains the theoretical long-term aim of the government: actual trends in the near future will depend on internal developments within the Soviet Union.

In agriculture, the proportion of livestock in private hands has been tending to fall for the last year or two, and this is likely to be accelerated by the recent reforms, with the accompanying reduction in the amount of land available for pasture. From the purely economic point of view the reforms are positive in nature, in that they recognise the distortions induced in the Russian economy by the lack of incentives in some sections of the collective farms' activities, and set out to rectify them by measures which will eventually bring about a better balance between the industrial and the agricultural sectors in general. But for some years at least, the additional resources made available by the price increases of June 1 will be absorbed in

essential capital developments designed to raise the present low level of productivity in agriculture, especially in livestock rearing, and will do little to reduce private enterprise proclivities among the mass of the peasantry.

With regard to housing, services, and the production of miscellaneous consumer goods, the trend will depend on what degree of relaxation is permitted in the present policy of giving priority to heavy industry and defence needs at the expense of consumption. Only to the extent that the state supplies the Russian people with the goods they want at reasonable prices will it diminish the urge to secure them at much higher prices through unorthodox channels, particularly as the complex system of incentive wages, to which state policy is pledged, will ensure that they have the means to do so. Moreover it is unlikely that at any time in the foreseeable future a highly centralised planning system, especially one oriented so strongly towards the non-consumption sector, will be able to satisfy all consumer demands in a varied and increasingly prosperous society. Assuming that human wants are not satiable, it may be anticipated that market influences will continue to operate throughout the Russian economy, in disguised or open forms, and that private enterprise will continue to satisfy consumer demands not met by the planning system, whether these demands relate to basic needs like food or housing, or to non-essentials like pop records and women's stiletto heels.

An economy like the Russian, dominated by politics and ruled by administrative fiat, inevitably tends to outgrow itself, and to develop what the economists call 'built-in deviations'. In industry, the hectic pace of

advance has created pressures to which the managerial class respond by the protective counter-measures of autarchy and the 'system within a system' of unofficial inter-enterprise relationships. The essential degree of slack in the economy which official policy refuses to grant is thus secured by unofficial means, and market influences which have been repressed reassert themselves in different forms. In agriculture, the peasants have clung to their private interests with a tenacity which so far has defied official pressures. The peasants have been carrying the whole country on their backs for centuries, for the sake of policies beyond their comprehension, and they have in consequence developed a rooted suspicion of all authority, a high degree of skill in the arts of evasion and self-defence, as well as a strong resentment of the inferior position allotted to them. The government's point of view must be appreciated: the peasants have always been so numerous and so important a part of the population that there have been no other shoulders on which the load could effectively be placed.

Recent reforms are unlikely to have any effect on this situation, for reasons that have already been stated. Nor is it likely that agricultural production will prove itself as amenable to exact calculation and planning as flights into space, or that administrative controls will succeed in overcoming the vagaries of nature.

The most remarkable transformation of all brought about by the Soviet government's economic policies has been in the Russian people themselves. Swift industrialisation demanded other material than a population accustomed to the slower rhythm of agricultural work, with a low standard of living and a high propor-

tion of illiteracy. To achieve their objects the government have perforce had to raise their people to a level of education and skill unknown in any previous period of their history. Having brought them so far into the light, it becomes progressively more difficult to push them back into the darkness of subservience, and already this new generation is exerting pressures for higher standards of living and greater civil liberties which the government are bound to take into account. The further emergence of this talented, profoundly patriotic and deeply pacific people, may well rank as one of the most significant and beneficent events of the twentieth century.

There is an essential similarity between the economic problems facing the Russian government today and those with which their predecessors had to deal. The Tsarist government was just as preoccupied as are the present rulers with the need to control and direct economic activity, not with a view to the immediate well-being and comfort of the people, but with the aim of strengthening the state and ensuring its safety in the future. The Soviet leaders have not escaped this basic dilemma of feeling obliged to pursue policies which are not as yet securely rooted in the conscious consent of their people, with the result shown in this study.

Another striking similarity with the past is the conviction that strong centralised control is essential for the preservation of the life of the state; hence the strength of the Tsarist belief in the divine basis of their absolute rule, and Soviet insistence that 'state discipline' must be preserved at all costs. This fear has deep roots in Russian history, from the 'time of troubles' in the late

sixteenth and early seventeenth centuries, when quarrels over the succession following the death of Ivan the Terrible threatened public security, as they did a century and a half later after the death of Peter the Great. Soviet rule has seen the alarming disintegration in the economy following the First World War, and the enormous increase in the acreage under private plots, with the consequent threat to the system of collectivised farming, after the Second World War. More recently, it looks as if 'localism' and 'drift' in industrial and agricultural management following the decentralising trends after Stalin's death have strongly underlined in the minds of the Soviet leadership the need for firm centralised control over the economy for a long time ahead.

Another inherited tendency which comes out strongly in present-day economic life is that of giving what Western thought would consider undue importance to questions of ideology and theory. Cut off from independent action by the autocratic form of government, Russia's thinkers have traditionally been driven back on theory and argument. In pre-revolutionary days, the Populist or Narodnik school of economists supported with the intensity of religious belief the thesis that Russia could by-pass the capitalist stage of economic development and go on directly to a state of socialism, as opposed to the Marxist doctrine, equally strongly held, which welcomed the advent of capitalism as a necessary stage on the path to socialism. The persistence of this attitude of mind explains much that is confusing and contradictory in the present economic scene: the insistence on a super-human standard of unselfish behaviour in economic life, while continuing

to lay great stress on the preservation of material self-interest; the expectation that national interests must always be given priority over local, while at the same time penalising industrialists for failing to fulfil a plan without ensuring them the requisite resources for fulfilment; the endless repetition of statements about the 'withering away' of the state, of the peasants' private plots, when manifestly nothing of the sort is happening. This is reinforced by another Russian characteristic, the tendency to believe that what they want to be true in the future is already true in the present, and that any deviations of today are a betrayal of the desired tomorrow. The key to the enigma is to focus less on the wall of dogma built up by these characteristics and more on the reassuring realities which go on behind the wall.

If similarity is the keynote in the nature of the economic problems faced by the Soviet government and their predecessors, it is equally prominent in comparing the practical working of the capitalist and communist economies. The administrative, technical and economic problems of running large industrial units are not affected by location or ideology. Problems of dealing with labour in conditions of full employment are not changed by differences in political beliefs. The Soviet manager may be more aware of controls from above, but in essence his task does not differ from that of a responsible official in one of Britain's nationalised industries or large privately-owned companies, or in one of the great American corporations. The basic laws of economics do not recognise political or ideological frontiers. On both sides of the Iron Curtain some measure has to be found which will enable scarce

resources to be allocated to their most efficient use, and obsolescence and rational price-setting are a necessity if serious economic inconveniences and losses are to be avoided. (When the planning and managerial reforms of 1962 are fully implemented, they will bring the functioning of the Soviet industrial machine a long step nearer the Western pattern.)

These similarities would be better understood if wider use could be made of the valuable work which has been, and is being done by professional economists who are also Soviet specialists. At present it remains largely unknown to intelligent non-specialist readers, who have no time to read lengthy treatises of up to 600 pages and who cannot cope with the mysteries of economic jargon. Economists tend to write for each other, or at best for students of the subject. Apart from books, much information of great interest is tucked away in periodicals with a limited circulation. It would help immensely to form a more knowledgeable public opinion if action could be taken to condense some of this useful material, put it into everyday language, and make it more widely available for policy-makers, business men, members of Parliament, and others who need to be supplied with information in concentrated form on the rapidly changing Soviet economic scene.

A useful result would be to help to dissolve the 'monolithic myth' which still dominates the minds of too many people. It persuades them to accept official Soviet statements at their face value, and to believe that in the economic sphere we are committed to a battle between two irreconcilable systems, a battle

moreover which the Russians are bound to win because of the inherent superiority of their system.

This is not only depressing, but is a long way from the truth. The Soviet system is not immune from economic troubles. To mention only one example, the present unbalance between agriculture and industry constitutes a grave threat to the country's entire economic life, and the Soviet leaders know that they will have to make immense efforts to overcome it. With regard to planning, it is clear that true competition with the free enterprise system, far from having been settled in favour of the Soviet system more than three decades ago, has hardly begun as yet. The Soviet authorities have shown that they can use their centralised power to develop large-scale industry to an impressive extent. They have yet to prove that, within the framework of a command economy, planning can be improved and refined to the point when its electronic computers can take over the functions of the 'invisible hand' of capitalist markets, and sustain a satisfactory level of efficiency. Collectivisation has been developed only as a method of extracting from agriculture the resources required to build up industry. It has yet to be demonstrated whether it can be made to function with equal effectiveness as a means for raising agricultural efficiency and productivity to the required levels.

It would be foolish indeed to minimise the danger that the power of militant communism presents to the free world. It would be no less foolish to ignore the truth that Russia's present drive towards greater economic strength is a deep historical necessity, and the natural desire of a great country to develop her human and material resources to the utmost. Given the differences

between Russia's social and political system and that of the West, this inevitable process would have made Russia an uncomfortable member of the comity of nations, whatever her form of government. If an exceptional degree of patience, wisdom and hard work is required to resolve the resulting differences, this should be regarded as part of the historical debt owed by the West to Russia, to which eminent scholars and historians like Dr Arnold Toynbee and the late Sir Bernard Pares have borne witness.

# THE POLISH ECONOMIC PENDULUM

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in association with

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## NOTE ON SOURCES

The material for this essay was drawn from both English and Polish sources. The latter comprised chiefly official statements in speeches at Party meetings and the views of unofficial persons such as professional economists.

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T.M.P.

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## I. A CENTRAL ECONOMY: THE FIRST STEPS

### HISTORICAL BACKGROUND

Between the two world wars Poland was occupied with two purposes. The first was political and economic unification: for more than a century it had been partitioned between three powerful neighbours, Russia, Austria and Prussia. The second was industrialisation. In 1921 nearly 64 per cent of the population, then 27.2 million, was engaged in agriculture, mostly at little more than subsistence level, while only 15 per cent was in industry and mining. The 1931 census showed that agriculture's share had fallen by only 3 per cent to 61 per cent of a population which had risen to 32.1 million. Demographically, therefore, the industrialisation drive had not been particularly successful. In the 1930s, however, despite five years of low production during the depression, the general index of production rose by about 20 per cent.

The war brought important territorial and population changes: about 70,000 square miles of territory in the east were ceded to the USSR while nearly 40,000 square miles in the west were taken over from Germany. The population within the new territory totalled only 23.8 million compared with an estimated 32.3 million in the same territory in 1939. But because of the inclusion of

highly industrial areas such as Silesia and Szczecin and the exclusion of a mainly agricultural area from Poland's territories, the reshuffle increased industrial capacity by about one-third.

#### SOCIALISATION OF THE ECONOMY

Post-war political changes in Poland brought to power a government dedicated to the establishment of a centrally directed economy. Its foundations were laid through a series of nationalisation laws and comprehensive economic planning.

Nationalisation of all basic industries other than construction but including public utilities was effected by a law passed in January 1946. Small-scale private industry, though permitted, was brought under control of the state through compulsory membership of state-directed associations. Nor did the co-operative movement, which had traditionally played a considerable part in Polish industry and trade, long remain outside the reorganised public sector. Under legislation of May 1948 the Ministry of Industry and Trade became directly responsible for the integration of the co-operative sector into the national economic plan.

The devastation and dislocation left behind by the war demanded what was described as a great and shared effort from all in the task of reconstruction. The task was difficult for all European countries devastated by war, but Poland had to refuse Marshall Aid and by contrast was used by the USSR as a cheap source for many of its needs; for example, Polish coal was exported to Russia at very low prices. In these circumstances the state rapidly took powers to mobilise and direct the entire national labour force, principally

through a decree of January 1946 which obliged everyone except the professional and agricultural cadres to register at state employment offices. These offices were empowered to compel persons registered to accept work of a type and at a location considered suitable; failure to comply could lead to a five-year term of imprisonment. Later the professional classes were also made liable to direction.

Although private ownership of land was largely retained, the amount of land any one person might possess was limited. Owners of large holdings were expropriated and their land distributed amongst landless peasants, who thus became tenants of the state. By the end of 1948 slightly over 100,000 farms amounting to 3.1 million hectares were expropriated and two-thirds were divided into small plots, the remainder being taken into direct state ownership and control. In addition, 60 per cent of the 6.7 million hectares of farmland in the recovered territories under government administration were allocated to individuals, the balance again being taken into direct state administration.

Although by 1949 about 90 per cent of agricultural land remained in private hands, the state was able to impose its policy of gradual collectivisation through the allocation of fertilisers, agricultural machinery and credit. Its powers of taxation were also used to discourage the larger, more successful farmers and to encourage the smaller farmers to join producer co-operative farms (collectives). During the years 1951 to 1955 decrees requiring farmers to deliver to the state grain, potatoes, meat and milk, were issued – demands made necessary by the food shortages among the

rapidly growing industrial population. As an inducement to collectivisation, higher quotas of compulsory deliveries were imposed on individual farmers than those demanded from collectives.

Because of such discriminatory devices a measure of success in the collectivisation drive was achieved: by 1953 about 7·2 per cent of farm land was owned by collectives while 12·8 per cent was farmed directly by the state and the remaining 80 per cent by individual farmers. Thereafter the pace of socialisation of agriculture slowed down; in 1956 77 per cent of agricultural land was still in private hands while towards the end of the year a wave of spontaneous decollectivisation, described later, swept the land.

Nationalisation of the banking system was a natural concomitant of the organisation of a centrally directed economy. Before the banking reforms of October 1948 a number of local and private institutions existed side by side with such state bodies as the National Economic Bank, the Agricultural Bank and the Postal Savings Bank. The 1948 reform liquidated the private sector in banking, and a decree of June 1951 placed the whole banking system under the direct supervision of the Ministry of Finance. The form of the system that then emerged was pyramidal. At the apex was the Polish National Bank, which prepared and carried out the financial plans of the entire economy; below it was the Investment Bank, the Agricultural Bank and the Municipal Bank, supplying their respective sectors with funds according to the plan and in addition acting as auditors to their dependent industries.

Banking relations with the public were entrusted to the General Savings Bank which dealt with transfers

of money by cheque as well as being a depository for the public's savings. Deposits in 1949 totalled only 46 million zloty, but by 1960 had risen to over 14,000 million.<sup>1</sup> During this period most foreign payments were controlled by the National Bank, though one of the two joint stock banks, the Commercial Bank, was permitted to engage in foreign transactions under the supervision of the Ministry of Finance. The other joint stock bank, the Polish Welfare Fund Bank, most of whose stock was held by the state, was also under the control of the Ministry of Finance.

#### THE EARLY PLANNERS

Thus through a series of nationalisation laws the state acquired control over the most important sectors of the economy. To exercise this control and give direction to post-war economic growth it established the Central Planning Board in 1945 under the supervision of the Economic Committee of the Council of Ministers. The Board was dominated by members of the Socialist Party – separate from the Communists until 1949 – and reflected its wish to maintain an element of private enterprise. In 1949 the Workers' Party (Communists) forced the Socialists to merge with them, and a number of the most prominent socialist leaders fled the country. The Central Planning Board was then replaced by the

<sup>1</sup> As far as can be ascertained from the meagre and incomplete statistical estimates published by the United Nations Economic Commission for Europe for the years 1949–53 and later figures made available by the Polish government, prices on the controlled market rose by 140 to 150 per cent between 1949 and 1960. Free market prices probably rose much higher. The purchasing power of the zloty therefore fell by at least 60 per cent.

State Commission for Economic Planning, which was given a larger role than its predecessor. Briefly its functions were:

- (1) to ensure the full utilisation of the potentialities of the economy and to prevent disproportion in its development;
- (2) to prepare in detail the national economic plans and to control and harmonise the plans of the various sectors of the economy;
- (3) to supervise and report on the fulfilment of the plans and to provide statistics.

The Commission was supported by the entire apparatus of the administration: the Sejm (Parliament) to which its plans had to be submitted and whose enactments gave them the force of law, the Council of Ministers – the chief executive body of the country – whose approval was required for their execution, and the Polish United Workers Party (PUWP) through whose labour and enthusiasm they would be fulfilled.

The detailed administration of a plan worked in the following manner. Having drawn up its national plan and obtained the approval of the Council of Ministers and the Sejm, the Commission would lay down the investment plans and allocations of raw materials for each industry. An industry received the finance necessary for the fulfilment of its share in the plan from the banking system which, unlike those of non-socialist countries, acted as an auditor and inspector to ensure that funds received were used for authorised purposes. Labour in the quantity or quality considered necessary could be directed to the areas of shortage. Its wages were paid partly in cash and partly in kind, a system necessitated by the dual price levels, those of the

socialised sector and of the private sector. In practice frequent adjustments of money wages or rations were needed to compensate the employees in the public sector for price movements on the free market since the rations failed to cover all the basic necessities. The system also led to complications for management, which had to price its supplies according to whether they came from the controlled or the free market. The workers themselves had little control over the management of their industry, for all decisions were made by the central authorities. The local peoples' councils, and the factory labour councils – administratively equivalent to western trade unions but in effect with little scope for looking after workers' interests: they had no right to organise strikes – were forbidden to interfere with the management. They did, however, meet the management at production conferences, an institution in which intention exceeded deed.

Quarrels or misunderstandings between industries of the socialist sector were dealt with by state arbitration commissions which could be called on to intervene by one or both of the disputants or could try to forestall a dispute on their own initiative. Any recommendation which an arbitration commission might make was binding on the parties to the dispute, subject to the right of appeal to the State Commission for Economic Planning.

#### LOCAL GOVERNMENT

Local government in Poland was entrusted to organisations known as peoples' councils. They were first formed in 1950 on a provincial, district and village basis, and they were meant to be responsible for the social and

economic welfare of the people in their areas. Education, housing, local revenue, expenditure and administration, regional economic and social planning and the control of industrial establishments (other than those directly subordinate to the central authorities), co-operatives (agricultural and non-agricultural) were administered by them. The councils formed a hierarchical structure: the village was subordinate to the district, the district to the province, the province to the National Council. Though each council was autonomous within its area it was required to co-ordinate its plans with those of the higher councils and with the national plan. Because of the highly centralised method of running the country during the first ten post-war years, the peoples' councils did not in practice have much authority or scope for initiative. They were used essentially as tools for carrying out the directives of the central authorities.

#### THE PLANS 1947-55

The period 1947-55 saw the implementation of two economic plans covering the years 1947-9 and 1950-5. The first was basically a reconstruction and recovery plan designed to put the Polish economy on its feet again after the devastation of the war. It attempted to develop the economy within a framework of three sectors, each of which it treated separately. The socialist sector was to be centrally controlled, the co-operative sector was responsible for drawing up its own plan within the framework of and in harmony with the national plan, and the private sector, though not subject to direct control, was to be guided in the appropriate direction by price and market regulations, by investment and

financial controls and taxation policy. The emphasis of the plan, which reflected the ideology of its socialist directors, was on decentralisation and minimum direct intervention by the state.

This policy, though successful, proved distasteful to the communists, who felt strongly that better and faster results would be achieved by a system which put more emphasis on centralism—a feeling reinforced by their conviction that the private and co-operative sectors were acting against the interests of socialised industry by attempting to gain speculative profits on the products of state industry.

The succeeding plan was therefore different in method, emphasis and objectives. The objective was the transformation and development of the economy on socialist principles, the emphasis was on centralisation, and the method showed strong Soviet influence. It called for the greatest possible exploitation of productive capacity and of technological progress, the fullest possible utilisation of the productive resources of the economy. The period was chosen to permit both the fruition of major investments and realistic forecasts.

Emphasis was placed on the primary importance of developing heavy industry in order to provide a firm and stable basis for the development and technical reconstruction of heavy and light industry, agriculture and communications. It was considered axiomatic that the development of heavy industry should precede the development of other branches of the economy and that the development of producer goods should outstrip the growth of the consumer goods industry. In view of these assumptions, it is not surprising that approximately 76 per cent of planned industrial investment

outlays were concentrated on the capital goods industries, a proportion which, as a result of steady upward revisions, rose to 89 per cent. Despite the fact that on many occasions plants were constructed without adequate regard to the supply of raw materials, such as minerals, the plan was over-fulfilled in this sector.

Plans to increase agricultural production were based largely on attempts to increase production per hectare through land improvement, drainage, flood protection and vermin control, and through a campaign for more research and training at all levels. But a combination of bad weather and lack of incentives for the peasants resulted in stagnation and decline after the first year of the plan, so that agriculture fell far short of even the revised targets.

The consumer goods industries, as one might expect both from the preamble to the plan and experience in other socialist countries, were to a large extent neglected. Their share in total planned outlay fell from 12 to 8 per cent, and their products were remarkable for poor quality and assortment, crude finish, bad packing and failure to meet consumers' tastes.

The results of the plan over the period as a whole were far from satisfactory. This became obvious to the authorities as early as the winter of 1953. The capital goods sector had become over-developed while light industry and agriculture remained seriously under-developed with grave effects on workers' morale. In the last two years of the six-year plan, 1950-5, the authorities revised their policies in an attempt to rectify the balance, though without much success. The effects of this disproportion in the fulfilment of the plan did not take long to permeate to the political sphere.

## THE CHANGE

The liberalisation which began in the political sphere in 1953 was reflected in the economy through a revision of plans in 1954 and 1955 aimed at improving the share of consumer goods in the national product. Throughout 1956 the authorities made efforts to ameliorate the lot of the workers, being influenced in this aim by the twin pressures of workers' agitation for higher pay and the changes of policy in the Soviet Union after the death of Stalin. In May the level of minimum wages legally provided for was increased from 364 to 500 zloty per month and was followed by an upward revision of pensions. Small-scale private enterprise was once more to be encouraged in order to overcome the painful shortages of consumer goods. In early October price reductions of several categories, including shoes, textiles and some household appliances, were announced. Meanwhile, farmers were showing their dissatisfaction by refusing to collect crops and deliver them to the state for nominal prices, so that serious food shortages developed.

Such was the economic plight of the country when, at the eighth Plenum of the Polish United Workers Party in late October, 1956, the more liberal wing headed by Wadyslaw Gomulka assumed almost complete control. The discredited State Commission for Economic Planning was quickly abolished and replaced by the Planning Commission of the Council of Ministers which was to administer a substantially decentralised economy. The exact method of decentralisation or, in the current terminology, the creation of 'a new economic model', was still in the course of development.

Meanwhile the crisis which overshadowed the economy had to be tackled immediately.

In December 1956 the plan for 1957 was drastically revised, eliminating investment in long-term projects and reducing those which would absorb large quantities of building materials and imported goods. On the other hand, residential building and consumer goods production were to be increased above the level envisaged in the original plan. Individual farms were no longer to be discriminated against in the allocation of fertilisers, machinery, and credits. Despite widespread disbandment of the collectives by the peasants, who returned to independent farming, the government retained collectivisation as its long-term policy. In the short run measures to encourage a rapid increase in agricultural production were introduced: compulsory deliveries of milk were abolished and quotas reduced and prices raised for grain and other products. These measures led to a rapid increase in the income of farmers. In the industrial sector, official policy was to increase the wages of coal miners only – a shortage of coal was causing industrial stoppages and an increase in unemployment. It was hoped that other workers would accept a wage freeze, and Mr Gomulka made repeated pleas to the population for patience and temporary acceptance of their low standard of living.

This approach was perhaps the best the government could adopt, for incitement to strike for higher pay was accepted as playing into the hands of the less liberal Stalinist faction within the party. Nevertheless a number of strikes took place during 1957 and several wage claims were granted.

## 2. DECENTRALISATION

### THE DEBATE ON 'A NEW ECONOMIC MODEL'

The whole method of planning was put under close scrutiny in 1955 and more particularly 1956 with the intention to decentralise it. The search began for a Polish way to socialism, although much of it was to a large extent simply a search for a theory that would take in changes already effected and set out general objectives towards which the economy might evolve in the future. Most important of all it was necessary to arrive at a theoretical model of an economy which had rejected centralism but was not to be permitted to dissolve into liberalism.

The questioning of past tenets of economic management erupted first in the specialised and later in the general press early in 1956<sup>1</sup>. Noted economists such as Henryk Fisz and Bronislaw Minc advocated the curtailment of the power of central government in economic decisions and the extension of the power of

<sup>1</sup> A new book by Professor J. M. Montias, *Central Planning in Poland*, Yale University Press, 1962, offers a most informative and enlightening survey of the events and disputations of this period.

local organs and individual enterprises. There were also arguments for changes in the pricing mechanism, such as Fisz's proposal that interest should be paid by state enterprises for capital allocated to them. The chief proponent of a price system which would more accurately reflect market conditions was Włodzimierz Brus. At a conference of economists in June 1956 his speech calling for such a reform made a big impact. Oskar Lange, who made the opening and closing addresses, first put forward a much more orthodox set of ideas which were modified during the course of the conference to bring them into line with the general call for decentralisation.

Towards the end of 1956 a new body, the Economic Council of the Council of Ministers, was set up to prepare the theoretical foundations for the reforms in economic administration and to advise the government. The Council sat under the chairmanship of Oskar Lange and many of the foremost economists, such as Czesław Bobrowski, Michał Kalecki, Włodzimierz Brus, and Józef Pajestka, were members. The Council formed a commission on the economic model which presented its recommendations, called 'Theses on changes in the Economic Model',<sup>1</sup> in July 1957. They were essentially a compromise between those who wished to see a revival of the use of markets and prices as economic regulators and those, such as Michał Kalecki, who had little faith in their efficacy at that stage.

The theses called for an improvement in planning methods through better economic analysis. Industry's plans, they said, should be achieved, first, through financial inducements and, second, through admini-

<sup>1</sup> *Życie Gospodarcze*, No. 22, 1957.

strative means. The targets of the central plans, except for basic materials, should be in value and not physical terms; central allocation of materials should be reduced gradually except for articles in short supply. The assortment of goods produced should in general be determined by the individual enterprise, profitability being the yardstick, but administrative orders should also be taken into account. Material incentives should not be tied to output; enterprises should pay interest on investment grants; the use made of the depreciation allowances should be determined in general by the enterprise, which should also have more scope in allocating the wage fund. Finally, the price system should be revised to eliminate the wide divergence between producers' and consumers' prices, and a new set of producers' prices should be worked out to reflect unit costs, particularly of the most important enterprises, and correspond more closely with world prices. The spontaneous formation of prices in a free market should not, however, be permitted.

The elaboration of price theory was continued by a sub-committee of the commission on the economic model. Its chief recommendations, put before the Economic Council in December 1957, were:

- (1) price changes should be restricted to intervals of several years;
- (2) domestic prices should conform more closely with world prices;
- (3) prices for all goods, except raw materials, should equal 'the average variable cost of "expensive" plants' which was considered an approximation to the marginal costs at which level output was optimum. If

shortages occurred prices might be raised, but it was preferable to try to manipulate supply and/or demand and maintain stable prices. Where efficiency within an industry varied widely from plant to plant, lower prices might be paid to the more efficient producers, higher prices to the less efficient.

The main criticism of the sub-committee's work, made at a conference on price theory in March 1958, was that it had not tackled the problem of long-run prices, fundamental for investment decisions. Indeed, after this conference little remained as evidence that a long and heated debate on prices had taken place. Price reform was left to the elaboration of the Planning Commission which had remained neutral in the debate and was concerned more with practical possibilities than with the twists and turns of theoretical controversy.

#### THE DECENTRALISATION MEASURES

The first decree extending the powers of the manager of an industrial enterprise was announced as early as April 1956. So long as he fulfilled a number of central directives the manager could use his initiative in allocating the depreciation and wage funds. He could inaugurate minor investments and increase sales above the planned levels. The new freedom most affected the private sector, which could now buy materials from state industry unhampered by the rigid controls imposed by the central authorities. This release from control perhaps accounts in large part for the increase in private building between 1955 and 1956. In 1955 the value of work executed by private enterprises and individuals amounted to 6,400 million zloty out of a

total of 38,200 million; by 1956 it had risen to 8,400 million out of a total of 40,100 million zloty.<sup>1</sup>

The number of decentralisation decrees increased considerably after the seventh Plenum of the PUWP Central Committee in July 1956. The resolutions of the Plenum called for decentralisation, 'more realistic' (i.e. less ambitious) production plans corresponding to available supplies of raw materials, and an increase in industrial stocks. (Lack of adequate stocks had been a major cause of complaints from workers because it often resulted in production hold-ups and loss of piece-work earnings.)

In August 1956 the responsibilities of the industrial central boards were widened by requiring them to determine norms of material consumption, except where enterprises did so themselves. A crop of measures was ratified in November 1956. They legalised the (spontaneously established) workers' councils, reformed the Planning Commission and extended the earlier decree which gave wider managerial autonomy to state enterprises in place of arbitrary and unlimited directives from the central authorities. They were now to fulfil annual plan indices stipulating the gross value of output, including the share to be marketed, production targets for the most important goods (after ensuring that sufficient materials distributed centrally were available to fulfil the plans), the total wage fund, planned profits or losses, the amount of profits to be paid into the state budget, the maximum value of

<sup>1</sup> *Concise Statistical Yearbook*, 1961, p. 73. I have included work executed by future users, private handicrafts and school workshops in 'private building'; in the source it is included in 'socialised building'.

investment expenditures permitted out of centrally controlled funds, maximum outlays on major repairs, and the enterprise's total of 'normalised' liquid assets.

In addition the managers were given powers to inaugurate 'sideline production' for direct sale to the consumer market at their own prices, to buy from the private sector, to initiate small-scale investments financed by bank credit and the enterprise's resources. More than a year later, in April 1958, the Council of Ministers issued a number of directives, including one empowering the enterprise to set up its own work norms, piece rates and bonus incentive schemes. The scope for initiating investments not controlled by the central authorities was also extended. At the same time the central boards of industry were abolished and replaced by associations of enterprises, i.e. legal entities which, unlike the central boards, were separate from the industrial ministries. They were to represent the interests of their members rather than simply transmit to them directives from the central authorities.

A number of measures were introduced in an attempt to make the profit motive the chief incentive to higher industrial production. Firstly, the role of the Enterprise Fund was extended. It is made up of a portion of the enterprise's profits out of which bonus payments to workers are paid and money for workers' housing is allocated. Up to 1957 it was of minor importance but the previously strict limits on the size of the fund were then removed, though payments from the fund were pegged at a maximum of 8.5 per cent of the total yearly wages. More important in encouraging the profit motive was a new bonus scheme for 'white collar' workers introduced early in 1960. These workers,

including managers, were to be entitled to a share from a basic bonus fund, allotted by the Ministry if production plans for the year were fulfilled. In addition, however, a separate fund was to be accumulated out of increased profits and divided according to proportions laid down by the Ministry. In this way the profit motive was to stimulate the managers' interest in the performance of their enterprises.

#### WORKERS' SELF-GOVERNMENT

##### *The legal provisions*

During the turmoil after the uprising in October 1956 when the general population thought for a time that it could take over the running of factories and farms, workers in industry throughout Poland spontaneously organised themselves into workers' councils on the Yugoslav model. The law of November 1956 making the workers' councils legal was passed under the pressure of events. The decree setting up workers' self-government conferences formulated at the end of 1958 was the result of long reflection. This, rather than the earlier law, can be said to represent the government's policy in this sphere.

The workers' self-government conference brought together the manager of the enterprise, the works' committee of the PUWP, the works' council (the TU branch), and the workers' council.

The executive arm of the conference is the workers' council. It executes the resolutions of the conference and supervises the management. It organises production conferences, controls financial and economic operations, decides on the obsolescence of machinery and similar technical matters, and endorses the enter-

prise's monthly and quarterly plans. With the works' council it decides the work norm and the system and level of wages.

The praesidium of the works' council gives opinions on the appointment of the management, controls trading with the private sector and the fulfilment of contracts with non-state enterprises. It plays a large part in the enterprise's labour relations, acting as a mediator between the management and the workers as well as deciding wages and bonuses.

The works' council is responsible for production plans and for enforcing laws concerning work safety. It also deals with welfare problems and such matters as sport, housing, etc.

Finally the works' committee, a party organisation, co-ordinates activity at factory level with that of the higher party echelons and is responsible for instilling socialist principles into the workers.

The conference as a whole gives its opinion on indices for annual and long-term plans for the enterprise to the local planning authority and endorses the plans in the light of state plans. It also decides on the investment of decentralised funds, on works' rules and on matters of bonuses, housing and so on.

#### *- and the practice*

Though the theoretical powers of workers' self-government have thus been made very wide, the whole question has ceased to be a burning issue in Poland. There is strong evidence that in a large number of cases industrial enterprises are still run on lines very similar to those of the 'pre-October' years. It would appear that after the end of the euphoria which swept the country

at the turn of the years 1956-7, when the people thought that their new leaders would at last bring them real freedom, the workers gradually lost interest in the management functions, which they had first appropriated and which were then legally thrust on them. Complaints at this situation are voiced frequently at party meetings. For example the report of the Political Bureau at the 9th Plenum of the PUWP central committee at the end of 1961 contained the following sentences:

'Many Party organisations and committees in factories have a tendency to substitute for the Workers' Self-Government organs, or to overlap their work, while the party bodies in the higher echelons fail to pay sufficient attention to this problem. Many factory problems which should be discussed by a wider group of Party and non-party people are dealt with only and exclusively by the management and Party officials or by commissions set up by Party organisations. In such cases the Workers' Council, its Praesidium and the conference of Workers' Self-Government only formally confirm problems which have been previously discussed and decided.'<sup>1</sup>

Party organisations within enterprises are often exhorted to allow more initiative to the non-party workers' representatives. Since they are almost in the same breath exhorted to be the vanguard of the country's economic development, it is understandable that they appropriate most authority to themselves. Such is not the case in enterprises that have an estab-

<sup>1</sup> Report of Political Bureau to the 9th Plenum of PUWP Central Committee, *Materials and Documents* (PAP), December 1961.

lished labour force with a generations-old tradition, as for example in the Cegielski factory in Poznan, where the demonstrations of June 1956 began. But the vast bulk of the Polish industrial labour force has come only recently from rural areas and has much to learn in the skills of organisation. The Party's appropriation of authority is, in these circumstances,

'simpler but . . . less effective as it weakens the workers' feeling of responsibility for their factory, closes up the outlet for sound initiative and criticism, closes the road to vigorous production activity and often weakens the ties between the Party and the workers'.<sup>1</sup>

#### THE ENLARGED ROLE OF THE LOCAL PEOPLES' COUNCILS

When the decentralisation policy was initiated in 1955, the peoples' councils were in a woeful state. The village and district councils were seriously understaffed, and the quality of the staff they had was low. The provincial councils were overstuffed and again the calibre was insufficient as the qualifications required were political rather than administrative or economic.

The need to change this situation was emphasised again and again by the authorities and every section of the population throughout the years of change. The first law (January 1958) to be passed considerably increased and expressly stipulated the powers of the peoples' councils. It provided for delegation of powers from higher to the lower echelons within the organisation. The councils were given more financial independ-

<sup>1</sup> *Ibid.*

ence – a move carried much further by a second law (July 1958). The legal basis was then gradually underpinned by more specific decrees of the Council of Ministers, as for example that which provided for the transfer of many industries from state to local government control. These included in particular enterprises which used local materials and/or produced for local markets, such as some branches of the food industry, light industry and enterprises producing building materials. In addition, the peoples' councils became responsible for the state farms, a considerable proportion of the road network, most of retail trade, much of primary and secondary education, and the public utilities within the area of their administration. The growth of the actual as well as the theoretical functions of the local authorities is shown by the growth in the peoples' councils' budgets from one-seventh of the state budget in 1956 to one-quarter in 1960.

#### SATISFYING THE CONSUMER

So much for the immediate and the ultimate authorities which run Polish industry. On what principles are entrepreneurial decisions made?

During the 3-year and 6-year plans the government concentrated its efforts on developing heavy industry and neglected light industry. After the 'thaw' efforts were made to satisfy to a larger degree the demands of the population for consumer goods. An attempt was made to create a link between the producers and consumer demand.

One effective but slow method was by studying changes in consumers' preferences. Since 1958 intensive researches have been conducted into family budgets.

This is done on a national scale and is still a long way from the elaborate market research carried on by private entrepreneurs in the west, but it is a pointer in that direction. A more sensitive gauge of consumer demand introduced into Poland in 1958 was the six-monthly Home Fair. Here the consumer goods industries show their wares and take orders from trading organisations. Trade is also being made more sensitive to consumer preferences by incentives such as commissions on sales, with larger commissions on sales of new products than old in order to stimulate development.

Though better results are now being obtained in satisfying the consumer than before 1956, it is still not unusual to find stocks of unwanted products soaring while shortages develop in other lines. This also happens in Western countries, but there free markets detect and put it right more quickly.

#### CHANGE OF EMPHASIS IN AGRICULTURE

Polish agriculture may, as we have seen, be divided into three sectors, the state, the co-operative and the private. Before 1956 policy was concerned principally with the expansion of the first two and the liquidation of the third. The excessive centralist tendencies of this period succeeded only in crippling the activity of the state farms whose output fell rapidly after 1948. The co-operatives or collectives also proved unsatisfactory for much the same reasons and because of the hostility of the peasants who disliked the coercive methods employed to induce them to 'co-operate' and the compulsory deliveries demanded of them when they agreed to do so. The pressures on private farms, both in the form of compulsory deliveries and difficulties in the

supply of fertilisers, etc., led to a decline in output in this sector also. The net result was that by 1955-6 a serious situation had developed in agriculture: discontent was widespread among the peasants, expressing itself in what one might almost call civil disobedience, and productivity had fallen below 1930 levels.

Faced with this situation the authorities introduced far-reaching revisions of policy. Collectivisation as a short-term objective was abandoned; instead it is hoped that the youth will be attracted by the relatively high industrial wages and the amenities of urban life and abandon their holdings, and that simultaneously the older peasants will be prepared to accept pensions in return for surrendering their land to the state. All in all the authorities envisage a lapse of 15 to 20 years before the time is ripe once more for a policy of collectivisation.

In the intervening period a re-orientation of peasant outlook and a spreading of socialist principles will be the task of the United Peasants Party (UPP) – the agricultural equivalent of the Polish United Workers Party. Party membership has tended to decline in the past few years. The Party is strongest in the central and eastern provinces of Kielce, Lublin, Warsaw and Bydgoszcz, and amongst the older peasants. It seems at present unable to attract the younger members of the farming community.

Of the UPP the most important sections from an economic point of view are the agricultural circles. These fulfil to a large extent the tasks of a co-operative advisory service but their activities are perhaps wider than those of the West. They provide not only courses of instruction in farm techniques such as care of

livestock, plant protection and so on, but also supply heavy machinery such as tractors, threshers, combine harvesters. They are officially described as semi-socialist co-operatives, and exist in 60 per cent of the villages of Poland; nearly half have a tractor and more than a quarter have two.

An extremely important aspect of their activity lies in the supply of credit. They are the sole channel through which peasants have access to a major source of credit, the Agricultural Development Fund. The fund, established in 1959, derives its resources from the difference between the price paid for quota deliveries and the free market price. These resources are at the disposal of the agricultural circles for collective investment on such schemes as irrigation projects, land reclamation and so on, provided the circles can prevail on the individual peasants to pay their share of the cost, which is calculated at 15 per cent in western Poland and 25 per cent elsewhere.

The other major sources of credit are the Agricultural Bank and the Savings and Lending Co-operatives. The latter, despite their name, derive most of their resources from state funds allotted to agricultural development; in the original 1961-5 plan they amounted to 28 per cent of the total planned investment outlays. Agricultural credit in Poland is divided into two categories: investment credits and turnover credits. Investment credits are normally granted for building operations, the purchase of pigs or cattle as stock, the purchase of machinery, or land reclamation. Except in building operations where the period is 20 to 22 years, they are normally repayable over eight years, though if a peasant leases his land to the state there is an auto-

matic 10-year moratorium. Turnover credits, normally granted for such purposes as the purchase of fertilisers, seed, fodder and stock for fattening, are usually repayable over 18 months and bear a rate of interest of 2 to 6 per cent. Contract-sellers, however, are not charged interest on loans, though the system of direct grant has now been abandoned except for sugar-beet and they receive their credits through the Savings and Lending Co-operative.

The contract system, which now extends to some 70 varieties of crops, fruits and vegetables, is an ingenious system by which the state is enabled to control trends in agricultural production as a whole and in particular regions. Under it the peasant agrees to supply the state with a stated quantity of a specified crop; in return the state undertakes to assist the peasant with credit facilities and the supply of fertilisers, chemicals, seed and machinery. The state, therefore, as a major supplier of equipment and credit and as an important purchaser of agricultural produce is able effectively to control the pattern of private agriculture. By and large the authorities take a pragmatic view of agriculture; the main objective is to raise agricultural production: where it comes from is relatively unimportant. They are in fact willing to sell land to the peasants from the Land Fund – state-held land arising from acquisition of abandoned or confiscated holdings – and in the past year or so the Agricultural Bank has been receiving some 2,000 to 3,000 applications per month from peasants wishing to buy land.

The co-operatives, better known as collectives, midway between the peasant and state farms, are perhaps the most productive sector of the agricultural economy.

The co-operative movement has long roots in Polish rural life dating back for over a hundred years. It fell into disrepute during the early fifties largely as a result of the coercive methods employed to induce peasants to join them. With the change in policy in 1956 their numbers declined. Many were broken up and their lands restored to the previous owners. At present the peasants are not coerced into forming co-operatives, though they are given strong economic inducements in the form of good credit facilities and high priorities for delivery of machinery, seed and fertilisers. Although they work in close co-operative with the village councils and the UPP they are independent of direct political control. Productivity in the co-operatives in 1960 was about 10 per cent higher than on the state farms.

State farms now embrace 12 per cent of the arable land. They have had a rather chequered history. They were established in the western territories and on some of the large estates during the post-war reconstruction, but scarcity of equipment and more especially of spare parts hindered their progress in the late forties. As these problems were being overcome, a further one appeared. In the drive to centralise and socialise the economy many of the qualified managers were replaced by unqualified political nominees, and the Ministry of State Farms tended to interfere in the management of the farms with the result that they began to make heavy losses.

In 1956, as in other spheres, agricultural policy was drastically revised. The Ministry of State Farms was abolished and unqualified managers transferred to more suitable positions. Managers, who now required high technical qualifications, were given freedom not only

to decide to a large extent what they would produce but also how it would be produced. They were to receive full market prices. The result of this enlightened policy was a rapid rise in productivity on state farms and a steady decline in deficits. But during the late fifties, despite substantial general progress, there was a tendency to diversify production excessively. It has been decided therefore that state farms will specialise in one or two products and will be formed into combines of several individual farms, each of which will produce one commodity and draw its needs of others from the other farms of the combine.

The purpose of the state farms is threefold: to produce better stock and better seed types, and to disseminate them among the farmers; to act as model farms where peasants can see the latest agricultural techniques demonstrated in practice; and finally to supply the state with agricultural produce. Substantial advances have been made in restocking and upgrading the quality of Polish livestock, particularly over the last five years. The quality of livestock is important, for 70 per cent of food exports are based on livestock products. Polish exports rely on their reputation for high quality and earn considerable amounts of hard currency, the six major markets being the United States, United Kingdom, West Germany, Italy, Switzerland and France. Intensive efforts are being made to enlarge these markets and funds have been allocated to projects for the improvement of packing techniques and the manufacture of special rail-cars.

The main problems facing Polish agriculture are the absence of modern techniques and of mechanisation on farms, particularly peasant farms (though the

extensive rural electrification programme and the expansion of the advisory service which is now in hand will go far to combat this deficiency), the mediocre quality of livestock, and losses suffered in the war. Gradually the problem has been taken in hand: the authorities have been importing large quantities of high-grade stock from the Netherlands, and establishing AI stations throughout the country. Another outstanding problem is the lack of fodder, despite intensive efforts to encourage its production. All in all, however, over the past eight years agriculture has not only recovered from the damage sustained in the war but has made very substantial advances.

Despite the external variations in agricultural policy, the basic aim underlying it has remained the same – that of ultimate socialisation. The change is simply in method, a realisation through experience that big changes are wrought only gradually. It is hoped that sound and healthy collective farms will be formed when – or if? – the peasants accept the ideal of working together in harmony for the common good.

This is the principle which underlies the Polish government's policy, both agricultural and industrial; the change, to repeat, has been simply one of method. Hence we find the emphasis on the work of the PUWP and the UPP, the need to instil the socialist ideals into the people. In method, pragmatism has replaced earlier dogmatism, patience former impatience. The social and political objective is a socialist society, the economic objective maximum productivity within this system. Methods are now accepted on results; in so far as the market system leads to higher productivity, the authorities accept it. They have shown a readiness to accept

the good in free enterprise while avoiding its pitfalls; this distinguishes Polish policy from that of many other socialist countries.

### 3. THE RETREAT FROM OCTOBER

#### THE ECONOMY AFTER OCTOBER

Having faced an explosive situation during 1956, the government set itself the task of improving the standard of living and thus lessening its political difficulties. The wave of unplanned wage increases during 1956 was to be avoided in 1957. To this end Mr Gomulka, who had the confidence of the population, made numerous speeches pointing out that strikes for higher wages would embarrass the liberal elements within the government and provide ammunition for the less liberal.

Nevertheless the average gross monthly pay in socialised industry increased between 1956 and 1957 from 1,320 to 1,578 zloty, or 19.5 per cent.<sup>1</sup> This increase compares with the 11.5 per cent rise, from 1,183 to 1,320 zloty, between 1955 and 1956. The 1957 figure, however, reflects increases near the end of 1956 which are only partially represented in the 1956 figure.

Pressure for a wage freeze in 1957 was thus evidently not successful, and in order to avoid an acute inflation

<sup>1</sup> *Concise Statistical Yearbook, 1961*, p. 57.

it was necessary to increase the output of consumer goods rapidly. The share of national income devoted to investment was cut in the 1957 plan to 19 per cent compared with 21 per cent in 1956 and 24 per cent in 1955. Production in both industry and agriculture was running at a much higher level than planned. The reasons were numerous and varied: the planned targets had been low, there was a general atmosphere of enthusiasm, increased stocks in industry allowed for smoother running of production, the harvest was good because of favourable weather and because individual farmers, assured of building materials, fertilisers, and higher prices for their products, made better efforts to increase production. In addition to these favourable conditions in the domestic economy, the government devoted an increased proportion of imports to consumer goods. Imports of agricultural products amounted to 16 per cent of total imports in 1957 compared with 12 per cent in 1956. Manufactured consumers' goods imports rose from 5.8 per cent to 6.4 per cent. The country was also flooded with packages of various consumers' goods from Poles living abroad who had now more confidence that such help to relatives and friends would not be confiscated in transit. As a result of all these trends the 1956-7 estimated rise in real incomes in the socialised sector amounted to 8 per cent (and of private farmers to 6 per cent).

In addition balance of payments difficulties, which by 1957 had become serious because of a fall in the volume and in the price of coal, Poland's chief export, were alleviated by substantial credits from both the eastern and western blocs. The USA extended a credit of 93 million dollars while the USSR cancelled Polish

debts amounting to 525 million dollars to compensate for 'trade irregularities' during the early 1950s.

During 1958 the economic policy of the previous year was generally maintained. The proportion of national income destined for consumption was to be slightly smaller than in 1957 – 79 per cent compared with 81 per cent – but was to be still quite high. Investment in agriculture, housing and social amenities, which had been badly neglected in the early 1950s, was also to remain at a high level. The planned rise in national income, 10·2 per cent, was about 1·5 per cent higher than that planned for 1957, but unlike it was far from being attained. Neither agricultural nor producer goods' production reached its target, and the over-production of consumers' goods could not be unloaded on what had become a buyer's market because of poor quality.

Towards the end of 1958 the economy ran headlong into another inflation. Its chief cause was not an absolute shortage of consumers' goods as in 1956, but a large expansion of decentralised investments. Local peoples' councils, state enterprises and production co-operatives had gradually been gaining a measure of financial independence and all were anxious to expand their activities. This resulted in above-plan outlays on wages and in a shortage of raw materials.

The situation was aggravated because 1959, according to the Five Year Plan, was to be a year of increased centralised spending on investment which added to the expansion of wages. Demand for food products, particularly meat, rose and farmers sold more for higher prices on the private market while deliveries to the state were 5 per cent lower than in 1958. Moreover

meat had become an important export,<sup>1</sup> and as a result a shortage developed particularly in the larger cities. A plenum of the Party's Central Committee was called in October to consider the situation and it was decided to raise official prices for meat by an average of 25 per cent in spite of the unpopularity of such a measure among the industrial working population.

#### RECENTRALISATION

The blame for the economic difficulties of 1959 was placed by Mr Gomulka on excessive decentralisation. From that point on the supporters of strong central control began regaining the upper hand within the economic administration. Limits were set on decentralised investments and enterprises were given more and more directives on how the wage fund and profits should be allocated. Specialised employees as well as raw materials were to be 'rationed' by the central authorities.

Workers' councils lost their appeal among the rank and file when it became obvious that they were being infiltrated by active communists and that their power could be only small when they formed merely one of the four components of the workers' self-government conferences. The associations of industrial enterprises, too, came to be the policemen for the central government – a reversal of their original functions.

Only the local peoples' councils are carefully cultivated by the central authorities. The entire 8th Plenum of the PUWP Central Committee in June 1961 was devoted to discussing methods of strengthening them.

<sup>1</sup> 100,000 tons of meat and meat products were exported in 1959 compared with 81,000 tons in 1955.

It has evidently been realised that the central authorities cannot work efficiently when they take responsibility for and authority over every detail of the national economy. Nevertheless, the peoples' councils are unlikely to embark upon activities not in keeping with the government's wishes.

## 4. PRESENT TRENDS

### THE ACHIEVEMENTS OF THE FIRST FIVE YEAR PLAN

During 1960, the last year of the first Five Year Plan, attempts were made to improve the balance of payments situation and to stabilise wages. To achieve these aims it was necessary to cut down the rate of investment growth to a mere 6 per cent compared with 17 per cent in 1959. Wage norms (piece rates) for a sector of the industrial population were made more stringent with the result that during the first half of the year there was a widespread decrease in real wages.

In spite of the cautious attitude to wages and investment and the continuing unfavourable balance of payments accompanying a worsening in the terms of trade, production increases in both industry and agriculture were quite high. Industrial production increased by 11 per cent over 1959 – more than in any other year of the Five Year Plan – while agricultural production was 5.4 per cent higher than in 1959. Moreover the continuing rise in rural electrification, in mechanisation and the use of fertilisers and in building provided a firmer base for increased productivity.

The results achieved over the whole Five Year Plan

1956 to 1960 were roughly in line with the relatively modest targets. The national income increased by 42 per cent over the five years instead of the planned 46 per cent. Gross industrial production rose by 58 per cent against a planned 49 per cent, gross agricultural production by 20 per cent against a planned 25 per cent. Real wages and agricultural income increased by 29 per cent, only 1 per cent short of the target.

#### A RENEWED ECONOMIC CRISIS

The Five Year Plan beginning in 1961 was thus launched in fairly stable conditions, but there was one major flaw. Agricultural production was still too low, with the result that heavy imports of wheat and other cereals were a burden on the balance of payments. On the domestic front, increases in industrial wages were spent on food. This increased the incomes of the chiefly private sector – the farmers.

In the first year of the plan (1961) climatic conditions were good and production was 10 per cent higher than in 1960 – a 6 per cent excess over the plan. Such a windfall did not, however, last long. 1962 proved disastrous – agricultural production fell by 8·5 per cent compared with 1961. Winter reserves of fodder for livestock had largely to be imported, while exports of agricultural products, which formed about half of total exports to 'hard currency' countries, were reduced. At a Trade Union Congress in November 1962, Mr Gomulka announced that a fresh impetus would be given to agriculture. Investments in 1963 were to be increased above the level provided for in the Five Year Plan, and during 1964–5 investments in the branches of

industry which serve agriculture would also be accelerated.

The objective of improving performance in agriculture has thus received first priority and is being tackled energetically. Other problems, however, continue, whether the economy is centralised, decentralised, or recentralised. They were enumerated in Mr Gomulka's speech of November 1962: waste of raw materials and manpower in industry, excessively long periods for completing investment projects, an insufficiently high quality of products which are not able to compete in the export markets.

The fundamental need of the economy has perhaps been best expressed in an interview with Professor Czeslaw Bobrowski published in the weekly *Polityka*.<sup>1</sup> He thought that the basic need was for education, so that workers at all levels, from unskilled to managerial, would be equal to their tasks. Once this is done, a further suggestion of Professor Bobrowski can be implemented – that enterprises should be given directives only once every five years, and that in the meantime the staff can work unhampered at improving techniques of production and quality of products.

It appears that the government is willing to test the efficiency of this 'revolutionary' method. Since mid-January 1963 over 30 enterprises working for export have had complete autonomy. If this experiment succeeds the implications will be far-reaching.

<sup>1</sup> The Economist as chief of staff' (Ekonista: Szef Sztabu), a conversation with the President of the Polish Economic Society, *Polityka*, No. 7, 1963.

# **STATE CONTROL AND COMPETITION IN YUGOSLAVIA**

*Ljubo Sirc*

## NOTE ON SOURCES AND ACKNOWLEDGEMENT

This essay is predominantly based on material published in communist Yugoslavia – books, daily newspapers, economic weeklies, journals, statistical yearbooks, etc., all of which are at least semi-official. Almost every sentence can be substantiated from a Yugoslav source, but many references have been omitted to avoid encumbering the text. All statistics should be taken as indicating general trends because of the general difficulty of calculating precise index numbers and other figures.

The conclusions are illustrated by quotations from authors living in the Federal People's Republic of Yugoslavia. Of these, Professors Mijo Mirković and Rudolf Bičanić are more independent-minded and outspoken than the rest.

The translation of communist language into English is difficult, because the communists have their own jargon which the Germans call 'Parteichinesisch' (party Chinese) which sounds strange in any language until one becomes accustomed to it. Sometimes I have had to use words with meanings somewhat different from those customary in English: the word 'enterprise', for

instance, is used to designate an economic unit under centralised and decentralised planning, but it does not imply private initiative as it does in a free enterprise society.

In this connection, I should like to express my thanks to Mr Jossleyn Hennessy for help in the preparation of an intelligible text.

L. S.

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## I. INTRODUCTION

### HISTORICAL

Yugoslavia was founded in 1918 by merging the Kingdoms of Serbia and Montenegro with the former Austro-Hungarian lands inhabited by the Southern Slavs. Despite considerable cultural and economic differences between the various regions of the new state, the constitution provided for a centralised government. There was, in consequence, much tension, particularly between the politicians and parties of the Orthodox Serbs and the Catholic Croats. Yugoslav Moslems from Bosnia and Catholic Slovenes who live in the North-West and speak a different though related language, tried to steer a more conciliatory course but were insufficiently numerous to play a decisive role.

In 1929, King Alexander abolished the parliamentary system and thenceforth ruled as an autocrat. After his assassination in 1934, a Council of Regents took over under Prince Paul. In 1939, the government signed an agreement with the Croat Peasant Party (representing the vast majority of the Croats), which gave autonomy to those parts of Yugoslavia in which Croats were in the majority, but this agreement was not recognised by the

Serbian democratic parties on the ground that they had not been a party to it.

Internal dissension was cut short by the war, when Yugoslavia was overrun by its neighbours Germany, Italy, Hungary and Bulgaria, and divided among them or parcelled out into small states under quislings. The small Communist Party of Yugoslavia, which numbered only 12,000 members before the war, succeeded in capturing the leadership of the resistance movement under the slogan 'brotherhood and unity for all Yugoslavs'. The various 'bourgeois' forces were unable to agree on a programme or a leader.

After the war, the communists silenced all opposition, democratic or otherwise, although they had promised to grant political freedom. Under the leadership of the Croat Marshal Tito, its Secretary General, the Communist Party, then numbering about 100,000 members out of a population of 15 million, introduced a people's democracy as a stage on the way to socialism, the first step towards a fully-fledged communist society. The Federal People's Republic of Yugoslavia consists of six people's republics – Serbia, Croatia, Slovenia, Bosnia and Herzegovina, Macedonia, and Montenegro – but since the Communist party applies the principle of 'democratic centralism' the term 'federal' has not the same significance as it has in the free world.

In 1948 Stalin expelled the Yugoslav communists from the international Communist Information Bureau (Cominform) because he objected to their independent spirit, their failure to obey his orders, and their efforts to start revolutions of their own in Greece and in Trieste. The expulsion isolated the Yugoslav left-wing from the communist world, and it was therefore obliged

to embark on a series of experiments of its own which have been of much interest to the outside world.

#### ECONOMIC

Yugoslavia has over 18 million inhabitants, of whom 7.8 million are Serbs, 4.3 million Croats, 1.6 million Slovenes, about 1 million Macedonian and Bosnian Moslems, and 500,000 Montenegrins. The rest are national minorities, of which the most numerous are 970,000 Albanians, 500,000 Hungarians and 200,000 Turks. Yugoslavia covers about 100,000 square miles (255,804 square kilometres) so that the average density of population is about 188 persons per square mile (72 per square kilometre).

There were sharp contrasts between the component regions of the Yugoslavia which emerged from the First World War. The standard of living in Slovenia was – and is still – about 50 per cent higher than the Yugoslav average and is comparable with neighbouring Austria. The level of development in the south-eastern regions is, on the other hand, far below the average, and is comparable to that in some under-developed countries. Despite the world economic crisis in 1929, Yugoslavia made slow but steady economic progress in the inter-war years.

After the 1945 victory, the Yugoslav communists sought to initiate a planned economy on the Soviet model. Their main principles were: abolition of private property in the means of production; the promotion of heavy industry; and all round detailed planning regardless of consumer interests. We shall see how this has worked out.

In the 1930s the working of a market under a socialist

system was the subject of prolonged academic controversy between socialist and liberal economists. Professor H. D. Dickinson, Professor Oskar Lange (the present chairman of the Polish Planning Commission), Professor A. P. Lerner, the late E. F. M. Durbin, and others wrote from the socialist viewpoint, while Professor F. A. Hayek, Professor G. Halm, Professor Michael Polanyi and others spoke for the liberals. But since there was no concrete example on which to base their arguments, the conclusions of both groups remained theoretical. Post-war economists have the advantage of the example provided by Yugoslavia, whose experience in the past ten years provides a useful economic laboratory. Yugoslavia's initial adoption of the USSR economic model and its subsequent transition to a socialist market economy show the practical difficulties in the working of the market under a socialist system. Moreover, since the Yugoslavs publish more detailed statistics than other communist countries, it is possible to assess what has happened with a reasonable degree of accuracy.

## 2. BREAKDOWN OF ADMINISTRATIVE PLANNING IN 1952

### RESTORATION OF THE MARKET

In 1952, the Yugoslav Government became concerned at the failure of the Soviet model to produce the desired results in the economy. The chairman of the Planning Commission himself, the late Boris Kidrić, exclaimed at the sixth Party Congress held in that year:

‘Who can guarantee that our plans are correct, if they are not submitted to the checks and correctives of objective economic laws? I personally cannot . . .’

The Montenegrin, Mr Svetozar Vukmanović, the communist leader responsible for economic policy, went so far as to declare that Yugoslavia’s economy had been planned ‘on an unrealistic basis’.<sup>1</sup>

Having made the discovery that economic laws could not be ignored indefinitely, and that central planning could not ‘liquidate the economic laws of commodity production’ which ‘broke through’ again and again, as a Yugoslav university text-book put it,<sup>2</sup> the Govern-

<sup>1</sup> Reported in *Vjesnik*, 1 January, 1953, the organ of the Alliance of the Working People of Croatia (formerly called People’s Front of Croatia), a communist front organisation.

<sup>2</sup> Miljević, Blagojević, and Nikolić, *Development of the economic system of the FPR of Yugoslavia*, Belgrade, 1956.

ment decided partially to liberalise the 'law of value' (the Marxist term for the law of supply and demand).<sup>1</sup> Even the chief planner, Boris Kidrič, declared himself in favour of 'the greatest possible automatism'.<sup>2</sup> Enthusiasm for 'automatism' went so far that in 1952 President Tito found it necessary to warn the Party that despite the 'freer functioning of economic laws', the fact of the participation of the workers in the administration preserved the Yugoslav system's 'socialist character'.

The Yugoslav leaders later retracted their admission of earlier error. In 1958, for instance, President Tito repeated the plea that it had been because of dire necessity that initially the economy had to be controlled from the centre in order to build up the socialist system.<sup>3</sup>

In fact, the re-introduction of 'the law of value' and of 'automatism' amounted to a partial restoration of a free market, called a 'socialist market'. This gave a new meaning to the system of 'workers' administration' adopted in 1950, but which had remained a dead letter

<sup>1</sup> By a coincidence it was also in 1952 that Stalin discovered 'objective economic laws' could not be replaced by five-year plans, and therefore reintroduced 'the laws of value' in his famous article on 'Economic problems of Socialism in the USSR', published in *Bolshevik*. This is one of the curious parallels which keep cropping up between the Soviet Union and Yugoslavia despite their ideological differences.

<sup>2</sup> Reported in *Borba*, 1 May, 1952, the Yugoslav *Pravda*. This newspaper had been the official daily organ of the Communist Party until 1954, when it was handed over to the Socialist Alliance of the Working People of Yugoslavia. At present the party (officially called the League) has no daily organ. 'Automatism' means 'giving up detailed planning and leaving the economy alone to work automatically via the market'.

<sup>3</sup> *Borba*, 28 December, 1958.

as long as the economy was planned and administered wholly by the central government. One participant at a meeting of Yugoslav economists in 1952 said that the effective introduction of 'workers' administration' had radically changed 'production relations'. The elementary functioning of the market now initiated proved to be a better regulator of the economic process than the most careful planning.

#### WORKERS' ADMINISTRATION

'Workers' administration' is not wholly independent of the Communist Party (now called the League of Communists) and its subsidiary organisations, such as the trade unions and the Socialist Alliance of the Working People of Yugoslavia. The Chairman of the Serbian People's Assembly, Mr Jovan Veselinov, explained in 1959 that the communists 'helped' the 'communes' and workers' councils to enable them to preserve their 'independence'.

Workers' administration consists of two elected bodies in each enterprise:

- (1) The 'workers' council', a larger body with mostly supervisory functions;
- (2) A smaller 'administrative committee', which constitutes the real management. This committee also selects the director of the factory after advertising the post, but the nomination has to be confirmed by the 'commune' people's committee.

The 'communes' are the basic territorial administrative units, named after the Paris commune of 1871. The elected body of the commune consists of two chambers, one elected on a one-man one-vote basis by the

people of the territory, the other ('council of producers') elected by those employed in 'economic organisations', i.e. enterprises. In the councils of producers, representation is not equal but according to individual 'value produced', so that the staff of capital-intensive factories, which produce more per worker than labour-intensive ones, is more strongly represented. Peasants who are not members of co-operatives, and professional people, are not represented.

The purpose of this system is to ensure the predominance of the 'proletariat', i.e. of the communists in the communes and in the higher administrative and legislative organs. In practice, the communists have other means, especially their monopoly of propaganda and power, to influence elections and decisions by the various bodies, so that they can get their way in matters to which they attach importance. In most cases the directors of larger enterprises are communists and they dominate the workers' administration in their enterprise. This is perhaps fortunate, because few workers understand economic developments; they are more interested in their personal earnings than in the management of enterprises. As Professor Mirković put it in 1959:

'In view of the present situation regarding productive forces, wages, and labour morale, workers' self-management can neither safeguard the common interest in the means of production, nor organise nor supervise production. In these circumstances the worker is much more interested in attempting to satisfy his individual requirements than he is in his functions as an independent producer, as a member of an enterprise, and as a representative of

the collective of workers entrusted with the means of production'.<sup>1</sup>

This explains the recent tendency of the workers' councils to leave the running of enterprises to experts and to concentrate on the well-being of the workers and the distribution of the net income.

Another aspect of the gap between the workers' administration and the enterprise is risk-taking. Professor Mirković wrote:

'The first question is who bears the risk. A capitalist entrepreneur suffers from his mistakes. He therefore does his best to ensure that his decisions are based on realistic assumptions. But under Socialism wrong decisions do not penalise those who take them.'

In capitalist countries, workers' wages are paid irrespective of the level of profits, and short-time working or redundancy takes the place of wage cuts. In Yugoslavia wages can be reduced if an enterprise is inefficient. The Yugoslav worker nevertheless enjoys a minimum wage, guaranteed by the state, irrespective of the fate of his enterprise.

Even directors of enterprises and other professional

<sup>1</sup> *Introduction to the Economic Policy of FPRY*, Zagreb, 1959. The author, a party member, is Professor of Economics at the University of Zagreb, Croatia. The importance of his book may be judged by the fact that it was published by the party publishing firm of 'Naprijed', and that the publisher's blurb said: 'The author does not claim to give a final and complete picture of our economy - such a task would not be realistic - but he makes a valuable contribution towards such a picture by tackling from new angles some essential questions of our present and future development, which he illustrates with lucidity. This book, therefore, is something more than a textbook for students of economics, though it will also serve this purpose'.

managers are exempt from the long-term consequences of inefficiency. They can find new employment without difficulty. In a speech in Split reported by *Borba* on 6 May, 1962, President Tito complained that, inefficiency apart, even people who stole five or seven million dinars (£2,500 to £3,500) were sentenced to a mere 18 months and thus earned more by running the risk of imprisonment than they could by 18 months' honest work. 'And after that these people are again appointed to some enterprise!' Inefficient managers can also claim that a loss was not their personal responsibility but a result of the 'economic system', or of its 'instruments', or of continuous changes in policy. To bring distributed profits in line with the increase in productivity, the Yugoslav communists avowedly aim at equalising conditions and at neutralising the impact of changes in the demand for the products of individual enterprises. The problem that emerges is how to run an economy on a market basis when the influence of the market on individual enterprises is eliminated.

In 1962 workers' administration was still the subject of contradictory views. Mr Kardelj spoke of the illusions which had prevailed about it. President Tito conceded that some people had had doubts about workers' self-administration, but added that these doubters had been 'replaced'.

#### LEGACY OF THE INITIAL CONCENTRATION ON HEAVY INDUSTRY

The introduction of the free socialist market in Yugoslavia was made particularly difficult by the economic policy that had preceded it. President Tito had laid down that under the 1947 Five-Year Plan

production was to ignore demand and profit; since it is an article of Leninist faith that socialism can be built only on the basis of large-scale heavy industry, economic activity was concentrated on investment and most investment went into the basic industries.

In 1957 Professor Bićanić commented in an English lecture in Tokyo:

'Preference was given to investment on the assumption of an unlimited demand for capital (and of unlimited reducibility of personal consumption which became a residual magnitude). All problems were supposed to be solvable only by new investment, and most of the attention of managing and policy-making personnel was diverted from problems of current production to those of investment. The consequences were often over-optimism in planned targets, installation of plants of over-sized capacity, and over-capitalisation in newly-built industries. The reasons for this attitude towards investment were first of all ideological, as if the building of socialism could be somehow measured by the spending of investment funds, and on the supposition that industries would create a working class.'<sup>1</sup>

According to the Five-Year Plan of 1947, investment should have increased to 3.5 times the 1939 level and absorbed 27.3 per cent of the national income in 1951. Instead of exceeding the pre-war total by 93 per cent in 1951, the national income rose by only 14.6 per cent over 1939 and returned to the pre-war level in 1952. The investment rate reached 28 per cent of the

<sup>1</sup> 'Economic Growth under Centralised and Decentralised Planning', in *Problems of Economic Growth* (Report of a seminar held in Tokyo), Delhi, 1960. The author is the Director of the Institute of Planning Research at Zagreb University.

national income in 1948 to 1950 but was far below the figures prescribed by the plan because the national income itself remained lower than forecast.<sup>1</sup>

The plan demanded very high investment rates and the concentration of investment on industry. Twenty per cent of the total investment went into social services and a little over 40 per cent was allocated to the fixed capital of heavy industry. But when the economic situation deteriorated in 1950, following over-optimistic planning and Yugoslavia's expulsion from the Cominform by Stalin (1948), the plan was revised: concentration on heavy industry was intensified, and plans for the consumer goods industry were dropped. This course was continued even beyond the five-year period to 1956. The planners realised that this created 'disharmony' between economic sectors but claimed 'that we consciously continued this disharmony so as to construct the key projects (i.e. heavy industry).'<sup>2</sup>

As a result, instead of the planned 52 per cent, an average of 58 per cent of investment (excluding social services) went into industry in the period 1947 to 1956, while agriculture, transport, and commerce were neglected. Of the industrial investment, 31 per cent was concentrated on power production (two-thirds on power stations) and 51 per cent on basic industries (iron and

<sup>1</sup> Figures about national income and investment are from *Jugoslovenski Pregled*, 1957, a monthly record of facts and information published in Belgrade under the supervision of an Editorial Board which includes the Director of the Federal Statistical Institute. The summarised quarterly edition in English is called *Yugoslav Survey*.

<sup>2</sup> *Slovenski Porocevalec*, 9 July, 1952. This newspaper had been the daily organ of the Socialist Alliance of the Working People of Slovenia, but was merged with the other Ljubljana daily morning newspaper.

non-iron metallurgy, machine building, shipyards, electrical and construction material industries) with emphasis on iron metallurgy and machine building. Only 18 per cent was left for consumer goods industries.

This concentration on heavy industries was financed to a large extent by disinvestment in agriculture and light industries, by over-exploitation of forests and ore deposits, and by inflation. According to Dr Nikola Čobeljić,<sup>1</sup> internal capital accumulation in 1955 amounted to only 15 per cent of the national income and not 23·6 per cent as stated officially; foreign aid and disinvestment in industry and social services accounted for the difference. Dr Čobeljić added that disinvestment in agriculture and in some social services (roads, canals, docks, etc.) had not been taken into account. He also asserted that inflation accounted for 16 per cent of nominal investment in 1955, i.e. that this proportion of investment was financed by the creation of new money.

'The inadequately large proportion of Department I [Marxist for "goods to be used in the process of production"] led to the freezing of resources, under-employment of capacities and a disproportionate increase in building costs.'

Unused capacities existed particularly in the new machine building industry. According to a publication of the Yugoslav Parliament, one of the weaknesses of rapid industrialisation was the 'insufficient use' of

<sup>1</sup> *The Economic Development of Yugoslavia 1947-1956 - Policy and Methods*, Belgrade, 1959, with an English summary. Dr Čobeljić is the Deputy Director of the Federal Institute of Economic Planning.

capacities. While the rate of use of heavy industry was given as 68 per cent, the accompanying commentary stated that most probably 'larger spare capacities existed' than were admitted.<sup>1</sup>

Dr Čobeljić said that the investment structure favoured large projects, so that the average number of workers per industrial enterprise in Yugoslavia was 266 compared with 128 in West Germany. Professor Mirković, too, referred to 'big manufacturing enterprises not all of which were economic under the present circumstances', and continued: 'They have another unfavourable characteristic - they destroy those small enterprises which are economic', because the communists tried to limit and destroy private enterprises, and 'small enterprises become unprofitable in a rigid and abstract collective economy'. Despite such criticisms, President Tito in 1962 advocated large enterprises producing 'basic and big things' while 'little things' should be left to socialist workshops.

Professor Mirković had doubts about the location of heavy industry:

"Slovenia has no bauxite deposits; yet the largest aluminium plant was built there. Croatia has only small quantities of iron ores, but a large iron works was built there, far from sea ports.'

<sup>1</sup> Quoted from Mirković, *op. cit.*

### 3. DISTURBANCES OF THE SOCIALIST MARKET

#### FORMATION OF PRICES

The disequilibrium brought about in Yugoslavia during the period of totalitarian planning made it impossible to work out economic prices and to find economic criteria for investment. Dr Čobeljić thought that as long as administrative controls continued, the price mechanism could not become a reliable instrument of cost accountancy for directing investment. The structure of the economy had been distorted and prices had ceased to have meaning.

When the free socialist market was introduced in 1952, newspapers reported numerous cases of unprofitability and losses in individual enterprises and, indeed, in whole sectors of industry. The uneconomic state of many enterprises had been hidden by the inflation of the previous seven years. Now enterprises were required to submit to the test of profitability, and the Yugoslav radio declared those who had doubts about the new policy to be 'cominformists and reactionaries'.<sup>1</sup> After a pause between 1950 and 1953,

<sup>1</sup> Radio Ljubljana, 19 May, 1952.

inflation returned stronger than ever because without it the newly-built industries could not make both ends meet.

The disequilibrium created in the Yugoslav economy after the war meant that 'free' prices existed only on paper; in practice they were frequently increased by arbitrary 'rates of accumulation' ('stopa akumulacije' – see below) and a high rate of purchase tax. In particular, consumer goods continued to be sold much above production costs so as to make possible the further financing of heavy industry, which was itself being paid subsidies per 'production unit' in order to boost sales. The leader in charge of economic affairs, Mr Svetozar Vukmanović, said in 1953:

'The machine building factories are entirely relieved of "accumulation obligations" [i.e., payments of interest rates and depreciation] . . . We are forced to pay them subsidies.'<sup>1</sup>

On the whole, the metallurgical and machine building industries, in which most had been invested, lived off the budget.<sup>2</sup> 'Refunds' ('regresi' – state subsidies to manufacturing or commerce to enable them to sell their products far below production cost) considerably distorted prices.

It was intended to replace 'refunds' by more up-to-date subsidies, credits, etc. But 'free prices' mean little if producers are subsidised. The central budget for 1962 provided the following 'allocations for special economic purposes' out of total federal expenditure

<sup>1</sup> *Vjesnik*, 1 January, 1953.

<sup>2</sup> *Slovenski Poročevalec*, 19 August, 1953.

amounting to about 550,000 million dinars (the national income in 1960 was 2,590,000 million dinars):

	<i>millions of dinars<sup>1</sup></i>	
	1962	1961
Refunds, bonuses and subsidies	98,935	76,360
Development of economic sectors	13,500	13,000
Refund of reduction in transport prices	6,200	12,000
Subsidies for export trade	45,000	50,000
Subsidies for investment in tourism	3,236	—
Repayment of internal loans	1,200	—
Repayment of external debts	<u>53,500</u>	<u>—</u>
	<u>221,571</u>	<u>—</u>

<sup>1</sup> At the rate of exchange introduced at the beginning of 1961:  
£1 = 2,100 dinars.

Most of these allocations are spent on power production and basic industries (although agriculture has recently had a share). In a footnote, *Jugoslovenski Pregled 1961* said that in addition to refunds, bonuses, and subsidies granted by the federal government, there were also subsidies in the forms of reduced interest on fixed and working capital, of written-off 'contributions on revenue', etc., as well as direct and indirect refunds and subsidies granted by local funds and budgets. It has also become customary (see below) not to repay bank credits, so that to a large extent they amount to yet another form of subsidy.

The indirect manipulation of prices did not last long in the socialist market economy. Prices began rising because of inflation and also because of efforts

to bring enterprises out of the red by requiring them to show a surplus over costs. It made no difference that the communist leaders then attacked 'the profitability at any cost' principle which was beginning to 'corrupt' some party workers.<sup>1</sup> The prices of some raw materials had been controlled from the early introduction of the socialist market, and in 1954 the central government decided to fix the prices of some final products. In 1956, according to Dr Čobeljić, the prices of 52 per cent of home-produced raw materials and 27 per cent of gross industrial production were controlled. *Jugoslovenski Pregled* 1961 said that 'ceiling' prices, introduced at first as exceptions, gradually extended to 50 per cent of industrial production.

Finally, the 1957 economic plan gave the government the formal right to control prices and even local people's committees were allowed to supervise retail prices. The Secretary of State for 'commodity circulation', Mr Marjan Brecelj, wondered in 1959 whether the price policy had 'a clearly defined place in our system'.<sup>2</sup> The Slovene Vice-President of the federal government and party ideologist, Mr Edvard Kardelj, summed up the current views of Yugoslav communists on market prices thus:

'When we speak about price control, some people ask if it is not contrary to the proclaimed principles of the free formation of prices and the free market. I think not. Our free market is a conditional term . . . It must be understood that the free formation of prices under our conditions means forming them

<sup>1</sup> *Slovenski Poročevalec*, 21 June, 1953.

<sup>2</sup> *Borba*, 1 January, 1959.

on the basis of supply and demand within the general proportions of the plan.'<sup>1</sup>

In his speech at Split in May 1962, President Tito attacked 'our business leaders who raise prices more eagerly and quickly than any capitalist', and he announced that a controlling body was being formed 'which would test whether increases in prices were justified, so that it would no longer be possible to raise prices irresponsibly'.

As soon as a relatively free market was introduced, monopolistic tendencies appeared.<sup>2</sup> This is not surprising: although factories are owned by 'society', the staff receives a part of the profits and therefore has an interest in raising prices. There were cases of division of markets and of price agreements. For a while these tendencies were resisted. It was laid down in 1956 that enterprises must not combine to conduct business jointly. Soon afterwards, however, business associations were officially introduced and even fostered. It was claimed that they had nothing in common either with capitalist monopolies or with the 'East European administrative monopolies', although their aim was described as 'the unification of production and marketing as well as the programming of production in common'. In 1960 there was much talk about 'merger mania' which, according to Mr Vukmanović, eroded the rights of workers' councils. But in 1962 President

<sup>1</sup> At the Second Plenum of the Socialist Alliance of the Working People of Yugoslavia, reported in *Borba*, 21 March, 1961.

<sup>2</sup> *Slovenski Poročevalec*, 17 February, 1952; see also Mirković, *op. cit.*

Tito again came out in favour of association and agreements between enterprises.

Before business associations were authorised, Professor Bićanić described the situation in Yugoslavia

'as an ambivalent system, partly governed by the laws of imperfect competition, and partly administratively controlled, so that it is very difficult to make this system work.'<sup>1</sup>

#### SEARCH FOR INVESTMENT CRITERIA

During the period of totalitarian planning, economic criteria of the profitability of individual enterprises had been ignored. Instead, the principles of planning were deduced from Marxist philosophy. As a consequence, investment loans were in effect gifts; no enterprise was under an obligation to repay sums advanced to it, or to ensure that it worked at a pre-determined marginal efficiency of capital. Sometimes, 'planned loss' was provided for, and this was not infrequently followed by 'unplanned loss'.

The introduction of 'automatism' required a more 'automatic' device for the accumulation of capital than the usual communist turnover tax, and a more realistic economic criterion for investment than Marx's *obiter dictum* that 'the mechanical means of production, which can be called the "bone and muscle system" of production' characterised each historical period of social production. Since the Yugoslav communists were ready to introduce a 'socialist market' but to give up neither

<sup>1</sup> *Progres* 1957, No. 9, a magazine published in Serbo-Croat, in Ljubljana, Slovenia. It disappeared after a year.

communism nor Marxism, they had to give this criterion a Marxist colouring.

At first they devised 'rates of accumulation', a levy expressed as a percentage of the 'wages fund'. According to Marxists, capital is not productive and may, therefore, not be credited with a payment. Any net income not allotted to labour is 'surplus value' or 'surplus labour', which should be related to the 'wages fund' and not to the capital invested. Hence the Marxist term 'rate of accumulation', corresponding to 'surplus value'; it bears no relation to any figure relevant to economic management and cannot be calculated in any scientific way.

In effect, 'rates of accumulation' merely reflected the situation in the Yugoslav economy in 1952. Since pre-war labour-intensive industries worked well, they had to pay high 'rates of accumulation', whereas the new communist capital-intensive industries operated at a loss and were therefore required to pay 'low rates of accumulation' or none. Even different enterprises in the same sector had to contribute different 'rates of accumulation'. The Banovići colliery, for instance, paid a rate amounting to 1,052 per cent of its 'wages fund', which was 2·5 times higher than that paid by the rest of the Bosnian collieries. Timber was much cheaper if felled by a commercial enterprise, which paid 65 per cent 'rate of accumulation', than if delivered by a timber enterprise obliged to pay a levy of 102 per cent of its 'wages fund'.

When it became necessary to adjust the 'rates of accumulation' to the market situation, the rate of the Laško wool factory was increased from 1,045 per cent for fabrics and 1,315 per cent for yarn to a unified

1,815 per cent. The 'rates of accumulation' for lorries, motor cycles and cinema projectors were on the other hand lowered because their rates had previously been so high that they could not sell.

At the end of 1952, Mr Svetozar Vukmanović said that the system of 'rates of accumulation' was 'too rigid' and that 'surplus value should be calculated in an economic way'. It was also suggested that 'under-developed enterprises' should be subsidised by straightforward subsidies rather than by lower 'rates of accumulation'.

Despite such criticisms, it was found necessary to retain the 'rates of accumulation' until the end of 1953. One of the main reasons was that no one knew how much capital had been invested in various enterprises so that a levy related to capital could not be calculated. Therefore in the first half of 1953 the value of fixed investment had to be established by estimates. Equipment was first valued in dollars, then converted into dinars. The cost of buying the equipment abroad was thus established, and the additional costs of producing it domestically were disregarded. In their own interest, enterprises tried to keep their estimates as low as possible.

In 1953 the centralised budgetary system of investment financing was abandoned and replaced by a degree of decentralisation and by a number of 'investment instruments' designed to achieve a more rational use of investment funds. It was laid down that investment credits must be repaid and interest paid on them. Investment funds were introduced and their administration handed over to the banks, which were required to check the estimates of future profits as well

as the 'social utility' of projects for which credits were sought. In Professor Mišić's view, these measures were successful in promoting efficiency and the rational use of investment funds.<sup>1</sup>

Professor Mišić's optimism was perhaps premature: the interest rate was hardly a 'deterrent' to waste by Yugoslav communist directors and their workers' councils because it was usually fixed too low. Moreover, according to Professor Vučković, it mattered little to an enterprise whether it paid an interest rate of 6 or 8 per cent; what it felt was important was to secure the credit at any cost. Experience showed that the enterprises in the most difficult financial situations offered the highest interest rates in order to make sure of getting the credit they wanted.<sup>2</sup>

Many managements acted irresponsibly. One director offered to borrow at 17 per cent; when asked how he could hope to repay a loan at this rate, he said that what mattered to him was to secure the credit; repayment was not his concern since he would no longer be in charge of the enterprise when it became due. The National Bank had to limit the interest rate to 7.5 per cent fearing it would otherwise be pushed up to 30 or 40 per cent.

Nevertheless the use of interest rates did bring some order into investment. This effect itself became a subject for criticism because heavy industry, the growth of which is so important in communist eyes, was the

<sup>1</sup> 'Investment and Investment Policy in Industry', published in *Ekonomika Politika FNRJ*, Belgrade, 1957, a selection of lectures given by high officials and university teachers at the seminar on the social system and international relations of the FPR of Yugoslavia organised by the University of Belgrade.

<sup>2</sup> 'The Role of Credit in Our Economy', *ibid.*

chief sufferer. The critics urged that the machine-building industry should be enabled

'to compete on equal terms with other enterprises, in particular with light and manufacturing industries, which can stand higher interest rates and shorter repayment periods because of their quicker turnover of capital.'

Dr Nikola Čobeljić published the following figures:

Industry	Gross investment per employed person (000 dinars)	Surplus value per employed person (% of wage fund)	Average income per employed person (dinars)
Electrical power	17,899	513	22,670
Iron metallurgy	8,360	603	23,440
Metal manufacturing	2,929	454	21,380
Shipyards	15,581	226	23,630
Textile manufacturing	855	785	16,380
Food	1,671	459	16,400

*Source:* The figures in the first two columns apply to 1956 and are taken from Čobeljić, *op. cit.*; the figures in column three apply to 1960 and are taken from *Statisticki Godisnjak*, 1961, the official statistical abstract.

If one assumes that surplus value is entirely composed of returns on capital (which it is not), one can calculate the following returns on capital invested in these key industries:

	per cent
Electrical power	0·65
Iron metallurgy	1·69
Metal manufacturing	3·31
Shipyards	0·35
Textile manufacturing	15·4
Food	4·3

This means that the returns on capital in the textile industry were 44 times higher than in shipyards, nine times higher than in iron metallurgy, 3.5 times higher than in metal manufacturing, and so on. It would also seem to follow that investment in shipyards and electrical power production in particular contributed nothing or very little to the Yugoslav national income.

Although the intention was to allocate resources for new investment to those who could offer the highest interest payments, this 'capital market' was soon divided into what were called 'auction circles without communication between themselves', the purpose of which was to ensure 'that investment funds were directed to those projects, or to those sectors, which help to implement our economic policy.'<sup>1</sup>

The new banking system introduced at the beginning of 1961 provides that banks 'must take account also of planning targets for the structural development of the economy'. In Split, President Tito criticised 'exaggeration in investment' and 'the tendency for everybody to build whatever he wants and whatever he likes' ('Sve što hoće i što mu se svidi'). He continued:

'Our banking system also has shortcomings. There have been cases in which those who could use resources profitably could not obtain them, while others – perhaps by bribery or other methods – obtained credits even though they could not guarantee to use them profitably.'

Professor Mijo Mirković has insisted that Yugoslavia must find an economic yardstick to measure priorities,

<sup>1</sup> Miljević, *op. cit.*

profitability, and productivity of investment. On the other hand, it seems doubtful whether the Yugoslav leaders understand what has caused so much trouble in their economy, since if they did they would hardly suggest that high costs and other problems of the economy, which uses excessive amounts of capital, can be solved by even more capital intensive electronic devices and automation.

#### LACK OF MARKET RESEARCH

The lack of real investment criteria in the past (as in the present) has led to what Professor Mirković described as

'the phenomenon that the supply of those products for which there was no demand was far bigger than the supply of those in demand. It was impossible to utilise fully the capacities in some enterprises because there was no demand for their products. On the other hand, there was, and still is, a very short supply of products in great demand, such as all kinds of food, textiles, housing, and transport services.'

No market research was done, or only superficial calculations based on population figures, regardless of present purchasing power and demand schedules, i.e. without taking into account the degree of development in the Yugoslav economy or the available national income per head.

Production of cars, radios, television sets, refrigerators, etc., was begun after 1955, although experience clearly showed that demand was concentrated on

necessaries. Since the size of the Yugoslav home market is limited by the predominance of low income groups, economies of scale are difficult to achieve. Most production is on a small scale, and costs remain high. In order to boost the sales of new products, their prices are kept down artificially, while the prices of more necessary goods are pushed up. Retail prices of textiles, for instance, were 33 times higher than before the war as early as 1951 – cotton textile prices even 53 times – although the general consumer goods price index had risen only 16 times. In 1960, a metre of ordinary cotton fabric cost 230 dinars against 8 dinars in 1939; a cotton vest was 792 in comparison with 37 dinars; and a metre of combed woollen fabric 6,147 dinars compared with 170 dinars. These high prices have meant that it has been difficult to sell textile goods, for which there is a high potential demand.

In spite of price manipulation, newly-built plants often work far below capacity. An investigation showed, for example, that utilisation of machinery in Belgrade plants is only 41 per cent of capacity in metal manufacturing and 56 per cent in electrical appliances, both figures based on one shift only. Even this degree of use is possible only because of a curious policy which allows credits to enterprises to enable them to build up stocks and continue their production even if there is no demand for their output, or grants credits to consumers – mainly other enterprises – to buy equipment they could not otherwise afford.

In view of the foregoing, it is hardly surprising that Professor Miloš Vučković believed 'credit is one of the most pressing of current problems in our economy,

in particular if stabilisation<sup>1</sup> of the market is desired'. Both Professor Mirković and Professor Vučković emphasise that repayment of credit is essential. Repayment is, however, not practicable, indeed impossible, if credits are granted to finance the stocking of commodities for which there is no demand or for the purchase of equipment likely to prove unprofitable.

#### INFLATION

The failure of the communists, obsessed by fixed investment, to provide working capital when they launch the construction of new plants increases their difficulties. When a new plant is completed, the management asks the bank for more money. More than once the government has tried to impose a credit squeeze, but it always provokes an outcry against idle capacities from the communist leaders themselves, and the government yields to public (communist) opinion. Professor Vučković said there was evidence that most short-term credit

'was used for capital accumulation and for contributions to investment funds; that a large part was used for fixed investment even though granted for short-term purposes; and that other credits were used to cover losses and other expenditure.'

These methods intensified the inflation which the government had initiated in its first administrative period when it financed investment and other expenditure by printing money. This inflationary policy was in

<sup>1</sup> 'Stabilisation' presumably meant 'a halt to inflation'.

line with the views of the late Boris Kidrič, the communist leader in charge of economic policy, who said at a meeting of the Economic Council: 'Tell me whether there is enough manpower. Don't worry about money – there's enough of that.'<sup>1</sup> The circulation of money rose from about 6,000 million dinars in May 1945 to some 50,000 million by the end of 1952, and to almost 250,000 million dinars by the end of 1961. It is claimed that the retail price index rose by about 32 per cent and the cost of living index by about 69 per cent between 1953 and 1961. Nevertheless Yugoslav communists claimed that inflation was impossible in a socialist system.<sup>2</sup> On 15 May, 1953, *Slovenski Poročevalec* said that inflation was only a passing symptom of Yugoslavia's fast development and could not be compared with inflation in a capitalist economy.

The volume of short-term credit also grows continuously. According to Professor Vučković it doubled between 1952 and 1956 from 457 to over 900 billion dinars. The volume of credit in fact amounted to 1,124 million dinars by the end of 1956, but was 'reduced' by turning the difference into working capital owned by enterprises. By the end of 1961 it had risen further to 1,427 billion dinars.

In spite of this expansion of bank credit, enterprises followed the generally accepted practice of granting

<sup>1</sup> Quoted in *Ekonomika Politika*, 10 September, 1960. *Ekonomika Politika*, published in Belgrade, is the nearest Yugoslav equivalent of the *Economist*, although it avoids articles of general interest and concentrates on economic matters, like the *Ekonomicheskaya Gazeta* in Moscow. In Zagreb there is another economic weekly, *Ekonomski Pregled*.

<sup>2</sup> For instance, Vice President Kardelj on 26 April, 1948, and the late Boris Kidrič on 25 April, 1948.

loans to one another and to administrative bodies without insisting on repayment. Profits were calculated on the basis of 'invoices issued' and not 'bills paid' and so no one troubled to exact sums due and all went to the banks for more money. *Ekonomска Politika* of 27 January, 1962, estimated that the claims of enterprises against administrative bodies alone totalled about 30 billion dinars. In the spring of 1962 the problem became so urgent that the government was compelled to order that all claims dating from before the beginning of the year should be cancelled through a clearing account at the National Bank. As a result, 1,500 economic organisations<sup>1</sup> in Serbia alone proved to be bankrupt – in deficit for more than 28 billion dinars. It then became a question whether to liquidate them or to grant them further credit to enable them to re-organise.

Until the beginning of 1961, inflation had been predominantly induced by the indiscriminate financing of investment; then new difficulties cropped up. Experiments with the distribution of incomes inside enterprises have been going on since the introduction of workers' administration. Until 1961, the government retained control of distribution by planning in what proportions income should be allotted to workers and for investment. In 1961, it decided that workers should be given a much freer hand in disposing of net income.

The new regulations laid down that from its total revenue each enterprise must first cover general expenses, the turnover tax, and the so-called rent, a

<sup>1</sup> The number of 'economic organisations' in the whole of Yugoslavia was 15,000 in 1959, of which about two-fifths were in Serbia.

levy on enterprises exploiting natural resources. General expenses include depreciation, interest on invested capital, and interest on credit. On the remaining revenue, the enterprise must pay a flat rate of 15 per cent to the central government. After this deduction, the workers' council is entitled to distribute the net income as they wish into a fund of personal income and a fund of the enterprise. Taxes on both funds are provided for: on the personal fund 13 per cent to various budgets (commune, district, republic), 24 per cent to social insurance, 4 per cent to the housing fund, and 1.5 per cent to the education fund.

The communist leaders hoped that the workers would prove responsible enough not to distribute more among themselves than was justified by the rise in productivity. They relied on communist cells in the enterprises to bring pressure to bear on 'less conscientious' workers.

In 1960, the average monthly wage of an industrial worker was 18,730 dinars (including his share in profits, amounting on average to less than 1,500 dinars). In pounds sterling this is £9 7s. (including the profit share of less than 15s. per month). Workers feel that these wages are low and they try to obtain more.

In fact, the new rule for the free distribution among themselves of net income led the workers (in most cases including Communist Party members) to press for higher distributions, so that at the end of 1961 the Federal National Assembly felt it necessary to pass a 'Recommendation on the distribution of the net income in workers' collectives', calling on the workers to rid themselves of 'the psychology of the salariat'. The workers were not impressed: in 1961, industrial wages

rose by nearly 30 per cent against a rise in productivity of about 7 per cent. The government therefore set up special 'commissions to implement the provisions for distribution of net income' to ensure their 'correct' interpretation. The official *Borba* drew attention to the discipline of Swiss workers, who did not push their wages above productivity.

## 4. SHORTAGE OF FOOD

### COLLECTIVISATION AND 'MECHANISATION'

After the Second World War, communist agricultural policy in Yugoslavia was, according to Professor Mirković, based on the assumption that 'it was possible to apply some Soviet methods in Yugoslav conditions', but he went on to say the authorities failed to realise that Yugoslav geographical, climatic and historical conditions

'differed from those of the USSR and that a higher productivity of labour already existed. . . . The system applied increased neither productivity nor production'.

The Vice-President, Mr Edvard Kardelj, thought that agriculture could not be organised properly 'so long as our peasant did not sit on the tractor', which was in line with Stalin's aphorism that 'the Soviet Union should be seated on the automobile and the *muzhik* on the tractor'. Extensive cultivation on the Soviet model was mistaken for technical progress.<sup>1</sup> Yugoslav-

<sup>1</sup> Extensive cultivation is the use of little labour and capital on vast tracts of land. Obviously it can be used only where the density of population is low, as in the USA, USSR or Argentina.

produced tractors and other agricultural machinery were so expensive that they were unprofitable. Their sales had to be subsidised heavily and their depreciation spread over an abnormally long period. Even so, in 1954 the cost of ploughing a hectare by horse was 2,000 dinars and by tractor 3,500 dinars.<sup>1</sup>

Obsessed by tractors, Yugoslav planners abandoned the complementary production of fertilisers when the economy ran into a crisis after the rift with the Cominform. The communists wanted to mechanise agriculture in order to free manpower for 'industrialisation', but heavy industry absorbed no less than one billion dinars to create employment for a mere 300 workers. Thus in 1960 the agrarian population was scarcely less than before the war. Yet there is an increasing number of officially admitted industrial unemployed, totalling about 200,000 in 1961. There is also 'surplus labour' in industry amounting to 15 to 20 per cent of the total industrial labour force of 1.1 million. There are, therefore, some 400,000 unemployed or uneconomically employed workers in Yugoslavia. In addition there is concealed unemployment in government services, which are often heavily overstaffed.

The basic objective of communist agricultural policy was not so much to increase or cheapen production as, in the words of *Das Kapital*, 'to destroy the pillar of the old society, "the peasant", and to replace him by the salaried labourer'. Nevertheless, the big drive for collectivisation started only when the Cominform accused the Yugoslav communists of favouring the

<sup>1</sup> *Ljudska Pravica*, 10 March, 1954. *Ljudska Pravica* was the official daily of the Communist Party in Slovenia. It merged with *Slovenski Poročevalec* in 1959.

*kulaks* – the rich peasants. An all-out campaign of ‘persuasion’ was accordingly launched. It was understood that ‘persuasion’ included ‘blows over the back’, as Tito put it at the Congress of the Croat Communist Party in 1948.

So disastrous were the results of this policy that the communists were forced to abandon it. In 1953 the peasants were given the choice of leaving or remaining on the collective farms; almost all who owned land left, even though this meant losing their cattle. This, said Professor Mirković, should be ‘sufficient proof that peasants did not enter collective farms of their own free will but were forced into them by compulsory agricultural deliveries and taxes’. Yugoslav authorities are agreed on this point.

Before the war, the land tax was 3 to 4 per cent of the peasant’s income. Under the communists it is from 10 to 20 per cent, though it was from 50 to 70 per cent when the pressure on the peasants was at its height. According to Professor Bićanić,<sup>1</sup> industrial prices in Yugoslavia were 81 per cent above the world market level in 1952 and agricultural prices 45 per cent below. Since even before the war industrial prices were 10 per cent higher and agricultural prices 20 per cent lower than on the world market, the 1952 industrial prices were some 140 per cent higher, compared with agricultural prices, than before the war. This means that the average money income of peasants before taxation, other things being equal, amounted to 42 per cent of their pre-war average money income.

Most Yugoslav authors agree that the sole result of the ‘squeeze’ of Yugoslav peasants was to impede the

<sup>1</sup> In *Problems of Economic Growth, op. cit.*

growth of agricultural production, and they attribute this failure to communist policy. President Tito himself said in 1953:

'We have not achieved what we wanted – more bread and more agrarian products. The opposite has happened; the production of all products has diminished'.

The hardship caused by this failure was all the worse in that the population had risen by 11 per cent between 1939 and 1955.

#### DE-COLLECTIVISATION

When Yugoslavia returned to partially free markets and the peasants were released from collectivisation they began 'to increase their livestock, to buy land and to invest, albeit in very small quantities and mainly from their earnings as industrial workers'. This description contrasts with the picture of collectivisation that Professor Bićanić had painted during the discussion on land reforms in Tokyo (published in the same book):<sup>1</sup>

'... the failure of collectivisation was so self-evident that it was impossible to carry on. After three years of that experience, it cost the country enormously in lower production and a fall in the rural birth-rate below that of the towns.'

Despite the welcome revival in agricultural output after collectivisation had been abandoned, their Marxist doctrine would not allow the communists to leave the

<sup>1</sup> *Ibid.*

peasants alone. They went out of their way to reduce the maximum holding of 20 to 35 hectares to 10 hectares, which is not enough for a Yugoslav peasant family to live on. According to Professor Mirković, this accelerated the flight from the village to the towns and industry. In addition, the communists tried to counteract the failure of the rural working co-operatives by forcing on the peasants the general purpose co-operatives, which had been widespread in Yugoslavia between the two wars.<sup>1</sup> This was not easy because their experience under the communists had led many peasants to distrust all co-operatives.

#### NEW SOCIALIST POLICY IN THE VILLAGES

In spite of these difficulties, Yugoslavia enjoyed a record harvest in 1959:

	<i>(Thousands of quintals)</i>					
	<i>Average 1930-39</i>	<i>Best pre-war year</i>	<i>Average 1948-57</i>	<i>1959</i>	<i>1961</i>	<i>1962</i>
Wheat						
and rye	2,642	3,287	2,439	4,395	3,360	3,720
Maize	4,300	5,340	3,510	6,670	4,200	5,270

*Borba* attributed this success to the Yugoslav socialist system, but it was rather due largely to the introduction of various types of Italian wheat, from which the yield per hectare was 2·5 times higher than that of domestic types, and to increased investment. 'Social investment' in agriculture had risen from 56 billion dinars in 1957

<sup>1</sup> In a 'working co-operative' land is pooled and peasants cultivate it as labourers under united direction. A 'general purpose co-operative' provides only ancillary services like marketing of products; the peasants remain independent and retain full ownership of their land.

to 107 billion dinars in 1960. The use of artificial fertilisers rose from 30,000 tons in 1939 to 450,000 tons in 1956 and to 1.2 million tons in 1960.

The big question is: what was the price that had to be paid for the record harvest? State farms and co-operatives had losses of 8 billion dinars in 1959, 14 billion in 1960 and 28 billion in 1961. The losses occurred in spite of 'refunds' to agriculture, or industry working for agriculture. The government paid subsidies, amounting to 25 billion dinars in 1958 and to approximately 31 billion dinars in both 1959 and 1960, to enterprises so that they could sell agricultural implements or fertilisers below cost. At the same time, while the 'social agricultural organisations' paid virtually no interest on their fixed and working capital, prices of their products never ceased to rise. In 1962, Mr Slavko Komar announced a further increase of agricultural prices by 45 per cent, intended to stop further losses by 'social farms', and an increase in taxation so as to prevent the private peasants from benefiting from the price increases.

Two Yugoslav communist precepts govern agricultural production costs. First, after their attempts to introduce extensive cultivation had failed, they refused to change over to the labour-intensive methods desirable in Yugoslavia's present conditions. They retain their enthusiasm for 'farms where human labour is almost entirely dispensed with'. Thus many more people continue to leave agriculture for industry than agriculture can spare or industry can absorb because, as *Borba* put it, 'the investment for improving the life of the people' in agriculture is in no way comparable 'to the enormous expenditure on machinery'. This

situation has been worsened during the last few years by state subsidies on the production of heavy machinery which replace much labour, while subsidies for smaller machinery and implements have been abolished.

Secondly, communist policy still seeks 'large-scale socialised production in agriculture'. Although the communists no longer attack individual smallholders directly, their aim is to eliminate them unobtrusively. This makes it necessary to concentrate available resources on smaller areas, which belong to the state, the co-operatives, and to peasants ready to 'co-operate' with co-operatives.

In 1959 713 kg. of fertilisers were used per hectare on 'social farms' whereas only 52 kg. were used on individual farms (including those of 'co-operating' peasants); in 1960 693 kg. and 54 kg. respectively. In accordance with the law of diminishing returns, the consequence is an unfavourable ratio between the input of resources and the output in yields. But Mr Slavko Komar denied the existence of the law of diminishing returns (because Marx had said it did not exist) and demanded that 'social farms' should not strive for 'medium'<sup>1</sup> yields but for the highest possible yields.

This policy aroused the distrust of the peasants. President Tito in 1959 and again in 1960 appealed to them to get it out of their heads that the government wanted to cheat them. That the peasants had reason for their mistrust is, however, suggested by Vice-President Kardelj's book *Problems of a Socialist Policy in the Village*,<sup>2</sup> in which he argued that the socialist sector

<sup>1</sup> He probably meant 'optimum'.

<sup>2</sup> Belgrade, 1959.

must be increased:

‘... for us the problem of socialist transformation of agriculture would be solved, by and large, if 30 to 40 per cent of arable areas could be encompassed by large-scale socialist production with high yields and high labour productivity. Then the socialist sector would absolutely dominate. . . . We shall still have a large number of independent peasants, so to speak agricultural “small craftsmen”, and private plots of various forms and acreage, but all these will no longer be important as economic factors. They will be obliged to co-operate unconditionally with the socialist sector and will be dependent on it.’

The communist ‘social farms’ continue to work at a loss, and in 1961 and 1962 the wheat and maize harvests were down to pre-war levels in spite of a 20-fold increase in the use of fertilisers.

Nevertheless President Tito in a speech in Split demanded the accelerated expansion of the ‘socialist sector’ in agriculture, which at present includes only 12 per cent of the arable area. The communists seem to prefer to produce large quantities of goods at any cost rather than those that satisfy needs at the lowest possible cost. Yugoslavia was once a food-exporting country; now it is importing about a million tons of wheat yearly despite the high percentage of its population employed in agriculture. Food imports largely account for the Yugoslav balance of payments deficit. The United States keep the Yugoslav economy going by supplying large amounts of their ‘surplus agricultural products’ as economic aid.

## 5. FOREIGN TRADE

### NON-EQUIVALENT EXCHANGE

In 1949, *Komunist*, the ideological journal of the Communist Party of Yugoslavia, published an article by Mr Milentije Popović, a member of the central government, about economic relations between socialist states. He argued that in Marx's view it was exploitation of a backward country by an advanced one if they exchanged goods at world market prices. Since labour was less productive in backward countries, different quantities of labour were being exchanged and not 'equivalents'. Trade would be socialist only if the less developed could sell its exports to the better developed country at a price above the world market level.

But this did not seem to be practical – even the Soviet Union took the view that 'trade was trade and friendship was friendship' – and it was therefore thought necessary in Yugoslavia to improve the structure of foreign trade by concentrating as far as possible on importing capital goods and equipment and exporting mostly finished goods that should fetch a better price for the labour incorporated in them.

The belief that investment in heavy industry would solve the problems of foreign trade continued to prevail in the 1950s: 'The completion of "key projects"

will completely balance the foreign trade deficit. We must import equipment for "key projects" worth another 200 million dollars', said the late Boris Kidrič in 1952. In the meantime, although equipment worth much more than these 200 million dollars has been imported, Yugoslavia's foreign trade deficit is higher than ever. On the other hand, since for a long time light industry had not been given foreign exchange to replace its worn out machinery, it has become necessary to import commodities that had been produced in Yugoslavia 30 years earlier.

Yugoslavia still seeks to change the composition of its foreign trade, particularly to export more and more finished industrial goods. Statistical abstracts give the following figures:

Class of goods	million dinars			
	Exports		Imports	
	1957	1960	1957	1960
Non-manufactured	37,458	43,609	70,419	50,000
Manufactured	49,158	65,668	45,876	56,364
Highly manufactured	31,917	60,571	82,099	141,552

These efforts to avoid being 'exploited' and to avoid 'any surplus labour being transferred', as Professor Mišić called it, resulted in exports at prices 'below the cost of production'<sup>1</sup> and 'at any price', which Professor Dragoslav Todorović declared to be 'against the general interest of our country'.<sup>2</sup> The gravity of the position is realised when it is recalled that Mr Svetozar Vukmanović

<sup>1</sup> Radivoj Davidović, 'Size, structure and distribution of the national income', *Ekonomika FNRJ*, Belgrade, 1957.

<sup>2</sup> 'Problems of our balance of payments', *ibid.*

said in 1953 that Yugoslav industrial prices were three times above the world level and agricultural prices 50 per cent below. Dr Nikola Čobeljić said that to earn one dollar Yugoslavia in 1955 had to export industrial goods worth 1,054 dinars compared with agricultural goods worth 655 dinars, while one dollar's worth of imported equipment cost 615 dinars and of imported raw materials 766 dinars. Although these figures may not be strictly accurate, the impression they convey about comparative costs is real enough.

Since 'highly manufactured goods', and in particular products of the machine building industry, cannot be sold to Yugoslavia's traditional trading partners in Western Europe, the government tries to divert part of its trade behind the Iron Curtain, to countries in the Middle and Far East and to South America, at dumped prices made possible by export subsidies. The 1961 budget provided 50 billion dinars and the 1962 budget 45 billion for this purpose. The United Nations *Economic Survey of Europe in 1961* reported that Yugoslav state aid to foreign trade is given 'mainly in the form of conditional and temporary tax exemptions'.

#### BALANCE OF PAYMENTS DEFICIT

Despite these special arrangements Yugoslav products, in particular equipment, often cannot compete with West European and North American exports, so that Yugoslav communists accuse their competitors of 'imperialism'.<sup>1</sup> Yugoslavia also began to grant commercial

<sup>1</sup> In this connection, the *New York Times* of 8 January, 1961, quoted the official Yugoslav bulletin in English, *International Affairs*, as saying that the United States was gradually taking over the heritage of the old colonial powers in Africa.

credits to customers in underdeveloped countries,<sup>1</sup> amounting, for example, to 100 million dollars in 1959. On balance, Yugoslavia received 9 billion dinars less credits in 1959 than it granted and repaid. On the other hand, Yugoslavia can obtain the products it needs only from the West, so that it runs large deficits with its western trade partners, especially Germany and Italy, and large surpluses with its communist and underdeveloped customers. These balances, even if they were equal, which they are not, could not cancel each other out because all Eastern trade is bilateral.

Although Yugoslavia had a foreign trade surplus balance during the last ten years before the war, amounting to 12.8 million pre-war dollars in 1937-8 (approximately 25.6 million post-war dollars), post-war trade has exhibited constant deficits, which reached their maximum in 1952 at 209 million dollars.

Between 1958 and 1961 the figures were:

	<i>Trade balance</i>	<i>Balance of payments</i>	<i>American aid</i>
1958	—48 bill. din.	—51 bill. din.	25 bill. din.
	—160 mill. doll.		84 mill. doll.
1959	—32 bill. din.	—47 bill. din.	31 bill. din.
	—106 mill. doll.		104 mill. doll.
1960	—72 bill. din.	—51 bill. din.	6 bill. din.
	—239 mill. doll.		20 mill. doll.
1961	—77 bill. din.		26 bill. din.
	—258 mill. doll.		87 mill. doll.

Exports reached their pre-war value only in 1958 in spite of the alleged large increase in net production.

<sup>1</sup> *Economic Survey of Europe in 1959*, United Nations, Geneva, 1960.

The extent to which Yugoslav exports were lagging behind was described by Hasan Brkić when he was chairman of the Foreign Trade Committee in 1957:

'The gross product of OEEC countries has risen by 48.7 points since 1948, their exports by 102 points. In Yugoslavia, social product had risen by 42.2 points from 1952 to 1956, exports by 27.2 points.'

According to the university textbook by Miljević, Blagojević, and Nikolić, exports amounted to 85 billion post-war dinars in 1938, while average exports in 1947-55 totalled only 65 billion dinars. Exports covered 82 per cent of imports in 1959, 74 per cent in 1960 and 62 per cent in 1961, excluding American aid. In consequence, Yugoslavia accumulated a foreign debt of almost 1 billion dollars, i.e. 750 billion dinars, about one-fourth of the national income.

#### NEW PROBLEMS FOR YUGOSLAV FOREIGN TRADE

During the last few years, Yugoslavia's economy has come up against new problems. The establishment of the European Economic Community has increased the difficulties of trading.<sup>1</sup> Yugoslavia is, of course, entitled to protest against discrimination and tariff walls, but the question is whether its foreign trade can be improved so long as the Yugoslav communists continue to run it on Marxist principles, insist on exporting goods that they are badly placed to produce and can dispose of abroad only with the help of subsidies or by dumping. The Yugoslav communists also have political reasons

<sup>1</sup> *Borba*, 14 January, 1959.

for disliking the European Economic Community. In 1959 Mr Kardelj said that the integration of Europe was particularly dangerous 'because it is based on the capitalist social system'. In a series of articles by Mr Janez Stanovnik, the Slovene director of the Institute of International Affairs in Belgrade, published in *Borba* in February 1962, European integration is decried as 'a new partition of the world market between capitalist industrial countries', 'a neo-colonialist form of continued exploitation of advantages', and 'consolidation of the capitalist West against the socialist East'. European integration has allegedly uncovered 'certain contradictions between the Western industrial countries', i.e. between continental countries, on one side, and the United Kingdom and the United States on the other. Since the communists consider that European integration constitutes 'an obvious policy of pressure on the working class', Mr Stanovnik appealed to European workers to unite with the peoples of underdeveloped countries to 'struggle for an internal change of the contents and substance of these efforts at integration'.

Simultaneously, Yugoslav government circles display enthusiasm, of which there was no trace before the appearance of the Common Market, for organisations like GATT and OEEC. In order to facilitate co-operation with international trade organisations, the Yugoslav government has passed a new customs law on the lines of western tariffs to replace the previous complicated system of unrealistic exchange rates coupled with a host of import levies and export subsidies called 'factors'. At the beginning of 1961, also, the exchange rate of the dinar was raised from 632 to 750 per dollar. But the new exchange rate did not help foreign trade

because the economy was not allowed to adjust itself to it; it is impossible for Yugoslavia to combine free trade with a policy of exporting 'highly manufactured goods'. It should concentrate on those goods which it can produce most cheaply.

## 6. CONCLUSIONS FOR INVESTMENT, CONSUMPTION AND INCOMES

### LOW EFFICIENCY OF INVESTMENT

The Table on the next page conveys a graphic impression of the results achieved by the Yugoslav economy under communist direction compared with the last pre-war year and after making allowances for changes in the value of money.

The almost 19-fold increase in the output of capital goods and equipment is not matched by a corresponding increase of the national income or of individual consumption. Before the war Yugoslavia imported machinery, but communist Yugoslavia, while continuing its import, produces much more at home, and generally invests much more. It was able to do this because foreign aid flowed in at the rate of more than £40 million per year, and through loans which have resulted in foreign indebtedness of £285 million. The figures therefore suggest that post-war investment was more expensive and its efficiency low. According to official data, the investment-output ratio amounted to

	(1939=100)				
	1948	1952	1956	1960	1961
Output of capital goods and equipment	352	582	971	1,789	1,861
Industrial production	150	164	266	451	483
National income	107	101	137	211	220(?)
National income per head	106	94	120	177	190
Individual consumption (1948=100)	76	70	81	118	126
Individual consumption per head (1948=100)	100	89	108	157	168
	75	67	71	99	105
	100	89	95	132	140

Sources: *Statisticki Godisnjak; Jugoslovenski Pregled*, 1957, pp. 465, 467, and 517, and 1961, page 403; *Economic Survey of Europe* in 1961. For individual consumption, *Jugoslovenski Pregled*, 1957, gave only figures for the period after 1948. Dr Nikola Čobeljić and Mr Berislav Šefer, *Living Standards in Yugoslavia*, Belgrade, 1958, simply equated personal consumption in 1948 and in 1939. Professor J. Marczewski, in *Planning and economic growth of people's democracies*, Paris, 1956, wrote of personal consumption after the war: 'In Yugoslavia, during the first years of five-year plan implementation, the rhythm of investment had considerably exceeded that of national revenue. The absolute margin between national revenue and investment had diminished to a large extent. And, if one takes the increase in inventories and in public consumption into account, personal consumption must have been much inferior to the pre-war figure.'

Professor Marczewski quotes the following figures from the *Economic Survey of Europe*:

	<i>Millions of dollars</i>		
	1938	1947	1948
National Income	1,040	880	960
Net Investment	52	132	144
	<u>988</u>	<u>748</u>	<u>816</u>

According to these data and according to my calculations, personal consumption in 1948 must have been approximately 75 per cent of the 1939 level.

10 in 1948-52, to 4 in 1952-6, and to 3 in 1957-60,<sup>1</sup> i.e. for the period 1948 to 1960 to at least 5.4. According to Dr Čobeljić, the marginal gross investment-gross output ratio was 5.7<sup>2</sup> and the marginal net investment-net output ratio 4.7 for the period to 1956. In 1962 the new chairman of the Federal Committee for Economy, Mr Boris Kraigher, said that the investment-output ratio had risen again, and that the national income actually decreased in 1961, although this statement is in conflict with official figures published later (see Table on page 178).

*Jugoslovenski Pregled* considered that this unfavourable ratio resulted from the structure of investment, which was such that in industrial production the relationship between the output of capital goods and equipment and the output of consumer goods changed from 30: 70 before the war to 63: 37 by 1956. The share of capital goods output in the gross national product will doubtless increase as the national income and the capital accumulated grow, but if the aim is to produce consumer goods at minimum cost the share allocated to capital goods and equipment will need to be held down. The communists however consider an increased ratio of capital goods output to be the prime objective of planning. The consequence is uneconomic use of machinery. The relationship between goods for production and goods for consumption in Britain was 48:52 in 1951, and consumption per head of population is several times higher than in any communist country,

<sup>1</sup> The data, including the repetition of the year 1952, are from *Jugoslovenski Pregled*, 1961.

<sup>2</sup> The same ratio for OEEC countries was 3 in the period 1947 to 1952.

even though large quantities of capital goods are exported. Indeed, this relationship applies to all British production, but the share of agriculture in its production is so small that it does not substantially affect it.

Wasteful investment on a large scale has meant that personal consumption has risen very slowly in post-war Yugoslavia. Although post-war investment as a percentage of the national income was several times higher than before the war, the rate of growth in 1947-56 was 4.8 per cent compared with 2.1 per cent in 1926-39. The growth rate falls to slightly less than 3 per cent if calculated from 1939 instead of from the very low 1947 level. The rate per capita was 1.9 per cent (1939=100) compared with 0.75 per cent before the war. Industrial output rose by 9.6 per cent between 1947-56, but before the war it was 10 per cent in 1935-39 and 5.4 per cent in 1926-30; it falls to 3.7 per cent if the crisis period 1931-4 is included.

The results in the growth of consumption were revealed by a member of the central government, Mr Milentije Popović, in the Federal Parliament in December 1957: personal consumption increased by only 0.2 per cent for each rise of one per cent in the national income. The latter increase was largely due to foreign aid. Consumption rose by only 4.2 per cent of investment, which means that the investment-consumption ratio was approximately 24: 1. These calculations are, however, based on the very low level of 1947. Based on 1939, total personal consumption had probably reached the pre-war level by 1958 and personal consumption per head by 1960.

## PERSONAL INCOMES

It follows from these figures that individual incomes have been very low since the war. Since the average wages of manual workers (including children's allowances) reached the pre-war level by 1955, when their number was 2·5 times higher than before the war, the incomes of the rest of the population (administrative staff, professional people, and especially the peasants) must have been much lower than before the war. These findings are confirmed by the statistics of labour productivity:

	(1939 = 100)	
	1956	1961
Industrial production	266	483
Industrial labour force	283	396
Value of capital used	348	—

Sources: Čobeljić, *op. cit.*, and *Economic Survey of Europe in 1961*, United Nations, Geneva, 1962.

By 1956, labour productivity in industry had fallen to 94 per cent and capital productivity to 76 per cent of pre-war. By 1961, labour productivity had risen by some 22 per cent compared with pre-war, while capital productivity had certainly remained very low, if it had not fallen. There are no recent data available about the increase in capital stocks, but it is known that the share going to investment in the gross social product remained at over 30 per cent.

The situation improved after 1956 because the 'social plan' for 1957-61 provided for changes in the structure of investment and for better utilisation of pre-war plants. By 1960, however, these spare capacities had been exhausted, so that 1961 was a disappointing year.

Industrial growth slowed from 15.3 per cent in 1960 to 7 per cent in 1961 instead of the planned rise of 12 per cent.<sup>1</sup> In May 1962 President Tito described the situation as critical.

There seems little hope that the increased capacities of the machine building and other heavy industries may trigger off a new phase of growth. Their equipment is both obsolete and worn out; the 1961-5 plan provides for their modernisation and reconstruction and for a new shift of investment towards heavy industry, in particular metallurgy.

In 1960 the manual workers' average monthly wage was 17,440 dinars and the average monthly salary of white collar employees 23,240 dinars. At the exchange rate introduced at the beginning of 1961, these incomes are equivalent to £8 14s for manual workers and £11 12s for white collar employees. The average monthly pay (including children's allowances) of a four-member family was 27,241 dinars (£13 12s) for wage-earning heads of households and 34,315 dinars (£17 3s) for white-collar workers compared with 978 dinars (£12 2s current value) and 1,857 dinars (£26 15s current value) respectively before the war. Since before the war there were no children's allowances except in government service, the pre-war average family incomes are fairly representative of the general average.<sup>2</sup>

The conclusion is that the average manual worker's family of four is slightly better off than before the war,

<sup>1</sup> *Economic Survey of Europe in 1961*, United Nations, Geneva, 1962.

<sup>2</sup> Figures on wages and salaries from *Statisticki Godisnjak* and, for 1939, from *Slovenski Poročevalec*, 6 May, 1952.

single workers and salary-earners much worse off. While re-distribution by means of children's allowances may be justified on social or demographic grounds, Dr Čobeljić has said that the widespread use of 'social allowances' neutralised wages as personal incentives. This is much less true at present than it was a few years ago because inflation has appreciably eroded the purchasing power of child allowances, which have remained unchanged. White-collar workers (especially if unmarried) are worse off than before the war. Senior professional people have suffered most. While a senior university professor earned £70 a month (at today's values) before the war, he now receives the equivalent of £25.

These salary figures include the participation in profits, which on average totalled 15 shillings per person per month.

Since the terms of agricultural trade had improved from 100 in 1952 to 157 in 1959,<sup>1</sup> the average peasant's money income, before payment of land tax, had (assuming he sold as much produce as before the war) improved to 66 per cent of pre-war compared with 42 per cent in 1952. While the pre-war land tax was 3 to 4 per cent of income, under the communists it has been 10 to 20 per cent and more.<sup>2</sup> These figures are fairly representative also of the rest of the independent population.

The Yugoslav communists have claimed that the Yugoslav national income per capita amounted to 280 to 360 dollars between 1957 and 1960. It would seem

<sup>1</sup> *Economic Survey of Europe in 1959, op. cit.*

<sup>2</sup> *Ekonomika Revija*, Ljubljana, 1951, the economic journal of Slovenia.

that they obtain these figure by dividing the nominal national income per capita in dinars by 410,<sup>1</sup> while the official exchange rate is 750 per dollar. The 1960 *Yugoslav Survey* gives 114,000 dinars as the national income per inhabitant. Divided by 750, this gives 152 dollars per capita. While this may be on the low side, per capita income is almost certainly much less than 280 dollars.

Since 1960, the nominal national income and nominal salaries have increased by a large percentage, but prices have also risen (20 per cent in the first four months of 1962 alone, according to *The Times* of 7 May, 1962), so that the exchange rate is currently calculated at 1,000 dinars to the dollar.

Since before the war the national income per capita was the equivalent of 115 post-war dollars, and since under the communists about 50 per cent of the national income goes to personal consumption (in 1939 at least 75 per cent) personal consumption per head at the beginning of the 1960s must be about the same as the pre-war figure. After 17 years of communist policies, the Yugoslav people are roughly back to where they were before the war. In contrast, consumption in the western world, especially in the lower income groups, has risen substantially.

#### THE ECONOMIC CRISIS OF 1962

In 1962, the Yugoslav economy was in crisis. President Tito first admitted this in speeches in May and June 1962, and the crisis was debated at length at a special session of the Central Committee of the Yugoslav

<sup>1</sup> *Jugoslovenski Pregled*, 1961, page 405.

League of Communists in July. The facts revealed were:

- (1) A fall in the growth of industrial production and stagnation in agriculture;
- (2) High nominal incomes and a continuous rise in prices;
- (3) A rise in commercial inventories, even of goods previously in excessive supply; and
- (4) Imports rising faster than exports.

During the life of the 1956 plan the Yugoslav economy seemed on the way to recovery from previous mistakes; the standard of living had been improving (with help from foreign loans). But in the 1961 plan the Yugoslav communists reverted to (Marxist) type: investment in general, and industrial investment in particular, was to be stepped up again, especially in those sectors which allegedly provide the long-term basis for modern industrial development (power, iron and steel metallurgy, chemicals, capital equipment, including electronics and automation). While the share of 'basic industries' in 'industrial investment' was down to 31 per cent in 1957-8, it rose again to 53 per cent at the beginning of the 1960s. In consequence, growth slowed down and then, it seems, stopped altogether, since the new chairman of the Economic Committee of the central government, Mr Boris Kraigher (a former chief of the Slovene secret police), said that the national income was falling. The growth of industrial production fell from 15 per cent in 1960 to 7 per cent in 1961 and to 4 per cent in the first half of 1962.

The Yugoslav communists changed the emphasis of the plan in 1961 because although they had decided

that the market might guide them in day-to-day decisions they held that fundamental economic development should not be 'elementary' (i.e. in accordance with the price mechanism) but should be based on the 'conscious social process of reproduction by planned direction'.<sup>1</sup> The emphasis, therefore, reverted to the uneconomic 'basic industries'. A member of the Central Committee, Mr Miloš Minić, thought that the disappointing development was due to 'the failures of our social plans, and to some bigger shortcomings and mistakes of our economic policy'. President Tito's contribution to the debate was the exhortation: 'Comrades, we should plan a little better!', and he added:

'I believe that we shall have to revise the five-year plan and our entire investment policy so that in future we shall invest only according to profitability.'

After 15 years of 'planning' a search began for 'a planning methodology' and a 'system for directing investment'.

It also emerged at the session of the Central Committee that in spite of increased nominal incomes, 92 per cent of employed Yugoslavs earned less than 40,000 dinars a month (less than £20). This led President Tito to ask how some working people were able to live on a mere 15,000 dinars a month (less than £7), and he complained angrily that in some factories the highest

<sup>1</sup> Cf. *Economic System and Economic Policy of Yugoslavia*, a collection of lectures delivered at the 'Political School', Belgrade, 1962.

salaries were 20 or more times higher than the lowest.

Winding up before the Central Committee, President Tito expressed his disappointment that the plenary session had not become a 'turning point in our economic policy'; few members had taken part in the debate; the chief reports were 'abstract' – they had nothing 'concrete to say about what measures should be undertaken'. He added that in the reports laid before the committee he 'could find no answer to the question how to overcome the present difficulties or how to run our economy in future'. The debates suggested that the Yugoslav communists are torn between Marxism and common sense. On the one hand, President Tito wants investment to be based on profitability, on the other, he told students of the Advanced School of Political Sciences that all conclusions 'must be based on Marxism'. This, of course, means priority for basic industries, which cannot be made to pay as long as they are launched on the scale hitherto attempted.

#### CONCLUSIONS

First, the Yugoslav example demonstrates the waste inherent in the Soviet economic model, whose pattern the Yugoslav leaders followed closely until 1952. On this point Professor Bićanić said forthrightly:

'To those who lived through it, the expense, in human and economic terms, of the system of centralised, bureaucratic normative planning is as obvious as the damage that it can inflict at all levels of the economy. Sometimes people, particularly economists, are led astray by the bias towards rationalisation, which leads to the superficial assumption that

centralisation means greater efficiency and speed. But competitive socialist planning, although it may cause some expense, is certainly cheaper than bureaucratic normative planning.<sup>1</sup>

Secondly, the Yugoslav experience suggests that the advantages of a market economy cannot be enjoyed unless the fate of entrepreneurs is bound up with the prosperity of their enterprises. In Yugoslavia, the personal economic responsibility of state managers and the workers' councils is non-existent or too diffused. In view of the economic situation in Yugoslavia in 1962 it seems that even one of the more judicious commentators, Mr Ernst Halperin, jumped to a conclusion when he wrote in the *Survey of Soviet and East European Affairs* of June 1962:

'The Yugoslavs have succeeded in refuting Wilhelm Roepke's dogma that private property is the indispensable pre-requisite for a market economy'.

It is idle to pay lip service to a market economy while refusing to accept free prices for consumer and producer goods. The economy cannot be liberalised if there is large-scale investment in unprofitable industries. It is difficult to inject reality into an economy after it has been long subjected to the wishful thinking of doctrinaire planning. The examples of Argentina and Yugoslavia

<sup>1</sup> Bičanić, *op. cit.*, p. 125. 'Normative' planning – as opposed to 'indicative' planning – is planning in which the government lays down 'norms' – targets for production without taking account of needs as expressed in the demand for various goods; 'indicative' planning tries to establish only what quantities are 'indicated' by economic development as forecast by market research.

are revealing. After mismanagement, major surgical operations are necessary. Yet without such surgery there seems no way forward. It is praiseworthy to seek technical progress, but advanced technology is economic only after an economy has reached a certain stage of development. If introduced too soon, it can slow down rather than promote progress.

Thirdly, Yugoslavia's economic development after 1945 suggests that the amount of investment is much less important than its economic use. On this point, Professor Bićanić said: '... had the plans for investment been smaller, more would have been built, and economic growth would have been quicker'. And Professor Mirković pointed out:

'It is not always correct to calculate production increases per head of the population compared with pre-war production. It is much more important to know what the ratio is between the amount produced and the amount invested, to know by how much production has increased in comparison with the resources that have been put into it. . . . It is clear that billions have been invested in different branches of the economy without increasing their production.'<sup>1</sup>

What the Yugoslav communists have achieved is the training of larger numbers of technicians than ever before, even though its quality has been low, while many children in central and south-eastern Yugoslavia are still without schools. The question is whether the necessary training could not have been given at a lower

<sup>1</sup> Mr Branko Horvat, an official of the Yugoslav Federal Institute of Planning, holds a different view - see Appendix, p. 191.

cost, and how valuable all this additional skill is if the system in which it is employed encourages waste. Professor Mirković commented:

'What is the use of many highly trained experts if their will is broken, if they have no feeling for what is economically possible, if they have no sense of responsibility, and if the conditions under which they work do not promote judgement and responsibility.'

In the light of Yugoslav experience, the leaders of underdeveloped countries may be less impressed by the high growth rates publicised by some governments; high statistical rates of growth often mean inefficient use of resources. They may perhaps ask whether the rational allocation of resources in accordance with the controlling power of demand, working through the price mechanism, will not provide the masses with a higher standard of living than spectacular investment in prestige projects. Rightly wedded to progress as they are, it may now seem more 'progressive' to them, and more advantageous in both material and human terms, to turn to the experience of countries like Japan, Germany, and the United States, whose predominantly market economies have given their peoples living standards among the highest in the world, without suppressing their political freedom or undermining their sense of personal responsibility.

## APPENDIX

In his paper, 'The Optimum Rate of Investment', in the *Economic Journal*, December 1958, Mr Branko Horvat said that 'a rational choice for the amount of investment is only possible in a planned economy . . . because it determines the rate of increase in consumption'.

Mr Horvat's views can be seen in better perspective against the following table put together from data given in the *Yugoslav Survey*, 1960, p. 35 ff.:

	s	r	k	rC
1923-39	4	2.48	1.7	2.48
1947-58	23.3	4.8	4.9	2.45
1947-58 (from 1939 level)	23.3	3.9	5.9	—

s = Net investment as percentage of national income.

r = Rate of growth of national income.

k = Capital co-efficient.

rC = Rate of growth of consumption.

It emerges that the communists almost doubled the growth rate by increasing investment more than five times. This result is even less impressive if the figures are taken from the 1939 level instead of the low 1947

level. Nevertheless, Mr Horvat would consider this result worth while merely because the growth rate has increased (regardless of the increased investment it required). If, however, capitalists had had a free hand in Yugoslavia they could have achieved the same growth rate as the communists by increasing investment by about 60 instead of 480 per cent. Yugoslav capitalists did in fact achieve this rate of growth before the war (except during the crisis years 1930-4). It is, of course, true that the capital co-efficient was diminishing in Yugoslavia in the 1950s, but this was partly because of the renewed use of capacities idle since before the war.

The picture is, however, very different if we consider the rate of growth of personal consumption rather than that of the national income. If 1939 is taken as the base year, there was no growth in personal consumption until 1958. With 1948 as the base year, the rate of increase was the same as before the war despite an investment five times larger, since we must assume that (unlike conditions in the communist production-orientated economy) the increase in consumption in the pre-war consumption-orientated economy was proportionate to the increase in the national income. Nor does this take into account the damage to the economy by communist disinvestment in many sectors, particularly in the production of consumer goods.

The figures quoted above do not suggest that the amount of investment is decisive, as Mr Horvat asserted, since the absorptive capacity of an economy obviously diminishes very quickly and the steep rise of capital co-efficients cancels out gains from the indiscriminate multiplication of investment. Mr Horvat pointed out

that a rate of growth of 10 per cent would, at his  $k=3$ , make possible a ten-fold increase of output within 24 years. He added that this was absurd and that there was a physical limit to the rate of expansion to which an economy can adapt itself. Is it worthwhile, then, insisting on an investment rate of 30 per cent when the inefficiency of investment will check the rate of growth? Communist countries have answered this question, since their experience is that the rate of consumption growth is out of step with the rate of growth of national income and with the rate of investment. 'The relatively slow expansion of personal consumption' is an established fact in the USSR and Yugoslavia alike. Communist economies are not only incapable of transforming high investment and growth rates into high consumption; they cannot discover (as a market economy does) what the real wishes and needs of the people are.

Mr Horvat himself believed 'that knowledge (and certainly not investment resources) was the most important scarce factor in underdeveloped countries with otherwise favourable social climates'. According to him, 'knowledge' comprises all skills, including scientific research. He does not refer to 'initiative' or 'economic responsibility'. 'Initiative' could be defined as the skill and the freedom of opportunity of entrepreneurs to discover directions in which economic ventures can best satisfy human needs, *whether in large or small enterprises*. Planners cannot fulfil this function, and they are moreover particularly apt to fight shy of small enterprises, even though they may be economically more viable than large-scale operations. 'Economic responsibility' provides the necessary link between the

success or failure of investment and the prosperity of the individual in charge of it; it compels entrepreneurs to select investment opportunities carefully. The absence of 'individual initiative and economic responsibility' seems to account for the high capital co-efficient in communist planned economies and for their low satisfaction of human needs. Planned economies are not, of course, compelled to indulge in the Marxist-Leninist concentration on heavy industry, but the lack of 'initiative' and 'economic responsibility' and especially unresponsiveness to the smaller human needs would probably also emerge in a planned economy even if it had an otherwise sensible investment policy.

The only conclusion, if any, that can be drawn from Mr Horvat's paper is that more resources should be left to entrepreneurs for investment, so that individual initiative and responsibility will enable them to use them to the best economic advantage of the community.

## **MARXIST FALLACY AND COMPETITIVE CO-EXISTENCE**

*Henry Smith*

## AUTHOR'S PREFACE

I have written this essay because its subject is one which appears to need discussing afresh with each successive generation. If there is little in it that is new, I make no apology, because the function of the economist is mainly to reiterate the obvious until 'practical' persons take notice. If competent Soviet economists were to comment on it I should be delighted, because the question is one which may be clarified by debate; there are enough solid differences of interest and opinion between communist and non-communist countries, and indeed within each group, for it to be worth while to spend some time in freeing them from the shadow of misunderstanding.

I am grateful to the Institute of Economic Affairs for providing me with a means of presenting, in a non-technical form, an argument which forms part of the theme of my book, *The Economics of Socialism Reconsidered*.

HENRY SMITH

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## I. INTRODUCTION

The thesis which these pages maintain is that at the foundation of the conflict between the main stream of communist opinion and that of the rest of the world (which could have destroyed us all before anyone reads them) there lies nothing but a series of erroneous economic propositions. There are also conflicts of interest; the interests of powerful and influential persons and institutions in the machinery of government, the 'establishment', on either side. There is the clash of interest between poor societies which produce primary products and wealthy societies which buy them. There is the age-old conflict within each nation between those, rich and poor but mainly rich, who wish to maintain the *status quo* (whatever it may be) and those, poor or rich but mainly poor, who wish to alter it. But these conflicts have arisen and been reconciled time and again, as part of the uneven pattern of progress. The economic dogma of the communists maintains that these differences arise inevitably out of the unalterable nature of a free enterprise society, that they are inseparable from it because it is basically illogical, and that they can be resolved only by its categorical destruction.

This assertion need surprise no one who has read

enough history to know how many wars have been wars of faith. But economics is a branch of science; one protagonist at least in this struggle disclaims faith, and claims that its policy is based upon a scientific foundation, the economic causation of history. If this is so the issue should be capable of clarification.

#### THE CORE OF MARXISM

Before clarification is possible, however, the kind of scientific logic upon which Marxism depends must be described. Contemporary scientific thinking in the modern world, in the social sciences as in other fields, is empirical in method, sceptical in temper. Those hypotheses which appear to offer the most generalised system of explanation of observed phenomena are provisionally adopted as working rules; the questions which any explanation has to answer are, 'Is it internally consistent?' and, 'Does it fit the facts better than its predecessor?'

This is far from the temper of Marx, the last of the great system-builders. A student of the philosopher Hegel, who saw the history of the world as a system of ideas developing through conflicts which reached agreement only to reveal new areas of conflict, Marx sought to turn Hegel upside down, or, as he saw it, right side up. For Marx the history of the world was the history of the conflict of economic classes, and ideas were primarily reflections of this conflict. Any society which produced more than was barely sufficient for existence would be dominated by the method of exploitation by means of which this surplus was concentrated in the hands of a ruling class. As technical and commercial changes altered the method of produc-

tion, the surplus would grow, the nature of the exploiting class would change, and the centre of gravity of the class war would move.

Thus out of the struggles engendered by feudalism, capitalism arose, replacing the battle between landlord and merchant for the rents of the peasant by the class war between capitalist and worker for the product of industry. This series of struggles must continue all the time that the product of industry was too small to permit a civilised life for all; it *could* end in the establishment of communism when the surplus was big enough for the necessity for conflict to disappear.

Considered as a hypothesis concerning the causation of the main trend of history, this view has been useful to many historians. In Marx's hands it hardened into the system of dialectical materialism: the foundation of what the Marxists term 'scientific socialism'. This is a tightly compacted philosophical system in which the history of human life and thought is regarded as the result of economic forces, interpreted strictly in accordance with Marx's ideas of economic analysis. It insists also that the change from one system to another must always be a revolutionary one, a clear and absolute break with the past. Often when Marxists make appeals to 'science' they mean conformity to this creed, which is essentially theological in temper. Critics of Marxist economics are referred to as 'bourgeois economists', mere reflections in the field of ideas of the existing distribution of property.

The core of dialectical materialism is the insistence that capitalist society contains contradictions which inhibit its continuation and which it is powerless to reform. Marx argues that the exploitation of the worker,

without which a capitalist society could not exist, leads to a distribution of income and a limitation of profit which makes the permanence of capitalism impossible. It is this which the communist economists must be capable of proving, in terms which do not depend upon the unqualified acceptance of the system of dialectical materialism, if their case is to stand.

#### THE BASIC ERROR

What the general run of communists appear to believe, to judge from conversations and the opinions of students, is something like this. All value is created by labour; the worker does not receive, and under capitalism cannot receive, all the value he produces. The fact of his exploitation by the owner of capital leads to constant over-production of 'values' which cannot be realised, and thus failure to use the creative powers of modern techniques. Thus the injustice of capitalism is also its weakness, preventing profits from being realised; capitalism creates powers of production which it cannot employ, and which a revolution leading to the employment of capital equipment for 'use' and not for 'profit' can alone release. Scientific economic analysis not only discloses the exploitation of the worker but also the historical necessity of a liberating revolution.

The basic error in their case resides in the labour theory of value. To say, as Adam Smith did, that labour is the foundation of all wealth is correct. To argue that the claim to a share in what is produced is founded more firmly on active participation in industry than upon the mere inactive ownership of land or capital is a moral judgement, which many would support. But the communist argument is that the aggregate value of economic

output, the 'quantity of value', which can be produced is determined by the quantity of wage labour, the 'socially necessary labour time', which is employed. Upon this they base their belief that if the amount of capital equipment in the world, which they say adds nothing to value, grows faster than the world's labour force, the rate of profit must fall, unless wages fall; hence the struggle of the classes must steadily intensify, and capitalism must either collapse or be transformed.

The essential weakness of this case is that the prognostications concerning the distribution of income between the different classes in society are not supported by any analysis of the forces determining the distribution of income which anyone with either knowledge of formal economic reasoning or with business experience can recognise as corresponding to what goes on in real life. For the communists all depends upon their prediction that, as capitalism develops, profits (including rent and interest) will be increasingly hard to maintain, except by progressively more desperate attacks upon the workers' wages. Why must profits decline? Not because real wages are rising at the expense of profits, which Marxists cannot or will not admit is possible under capitalism. If, therefore, profits cannot rise and wages cannot rise, where does the increased output of a developing economy go? The Marxists are forced to deny that it exists, or if it exists to assert that it is without 'value'.

Communists do not deny that capital equipment increases *physical* productivity, or, in other words, aids labour to produce more: indeed communist countries devote much of their resources to capital-building. But they maintain that, as capitalist production is wholly

motivated by profit, which they say is measured in quantities of 'value' and is not concerned with the growth of real wealth, the parallel increases in the stream of real wealth, in the form both of wages and profits, observable in the advanced countries, are only an irrelevant illusion. They further maintain that with the advent of public ownership of productive resources the potential, but suppressed, capacity of capitalist society to fulfil human needs will be released; production will become geared to 'use value' and not 'exchange value'. No Marxist economist has yet satisfactorily explained in what way this productive capacity is inhibited by private ownership, or how the release will take place. The whole system of thought depends on the assumed imprisonment of economic life in free enterprise societies within the (imaginary) fixed circle of 'value', and is fallacious. From it is derived an erroneous belief that there is an unchangeable, closely integrated economic and political system of capitalism, which ultimately must collapse, and an equally erroneous conviction that a socialist revolution will, by the mere transfer of the ownership of property to the state and by focusing economic policies rightly upon 'use' rather than 'exchange value', enormously increase productivity.

The basic error lies in maintaining that economic activity employing a given quantity of socially necessary labour time produces a fixed quantity of 'value', and that the way in which capitalist society measures the aggregate of all goods produced depends wholly upon the amount of this 'substance' which they contain. The argument collapses once this fallacy is abandoned in favour of the rational view that high productivity

per man-hour is the aim of economic policy and the test of economic success in all countries, and that the 'value' of goods is a *ratio* depending upon the relative difficulty of obtaining them, so that a fall in the market value or price of anything, reflecting greater ease in its production, is a social and economic gain.

The labour theory of value, in its two different aspects, lies at the basis of the present East-West conflict for two reasons, one moral, one economic. If labour alone creates wealth, and if the owners of land and capital appropriate much of it, labour is exploited. Regarded as a proposition in moral philosophy (and differences in this field are incapable of logical proof or disproof) it effectively divides the Soviet system from much of the rest of the world; but, so long as the conflict remains in the world of ideas, each country could be left to make its own decisions within its own political framework. This is the moral difference.

The second is economic. Marx claims scientific foundation for the proposition that labour alone creates *value*, arguing that while inventions embodied in capital equipment can add to the physical product of labour they add nothing to the value of output. Upon this is based the prediction that the class struggle must intensify, that the rate of profit must fall, that capitalist societies must ultimately collapse, and finally that the future of human civilisation depends upon their transformation into socialist societies before they break down. Upon this Lenin based the doctrine of the dictatorship of the Communist Party, the implication being that it is the duty of those who can interpret the inevitable trend of history to employ any means to save humanity from ruin. Once this doctrine is accepted,

negotiations between communist and non-communist countries become a farce. Why should a convinced communist do more than make such statements as seem expedient, in whatever situation exists, while waiting for the inevitable collapse of his opponent? It is this attitude on the part of communists, and the inevitable exasperation it provokes, which is the real point of danger. Yet it all rests predominantly upon a single basic error in economic analysis.

The controversy is an old one. Why go over it all again? Because of the enormous danger of the present situation; because the lessons inevitably learned by many communists in the process of their massive economic development must make them more receptive to economic logic; because developments in economic science in the West now make it possible to reduce the depth and frequency of those periodic depressions upon which the communists rely for empirical evidence to support their prophecies of doom; and, finally, because there are elements in the teaching of Marx, not wholly at variance with his basic philosophy, which could if given due weight make reconciliation possible without any humiliating renunciation of the true ideals of communism.

The course of the argument which will be followed is this. First, the ideas of the early socialists will be summarised and examined, because it is out of elements contained therein that Marxism developed. Then the Marxist system of economics will be examined, and the complex but monolithic structure of error it contains will be revealed, together with the one profound truth, now shared both by Marxists and by all liberal economists, that economic life free from bitter conflict and

harsh injustice can be secured only by the accumulation and utilisation of capital. The next section will show how, in the advanced free enterprise countries, *both* the accumulation of capital and its full utilisation (the possibility of which Marx denies) were possible and have taken place, and have diminished the harshness of economic life. The next two sections will explain the reasons why both in the West and in the Soviet countries the whole of the hopes of the early socialists have nevertheless not been realised.

## **2. THE OBJECTIVES OF THE EARLY SOCIALISTS**

Apart from the authors of the classical and medieval utopias, socialism is the child of the Industrial Revolution in Britain. Over a wide area customary institutions and the habits of mind they engendered were breaking down, the physical product of labour in the new factories was rising visibly, real wages were often stagnant or falling and, even when they were rising, were offset by the social degradation of life in the new towns and the indignity of unaccustomed factory discipline. Study of the literature of socialism makes it clear that the early socialists were after freedom from the economic constraints of poverty and believed it might be found in the collective ownership and co-operative utilisation of capital. To support this view they had to prove that social ownership of the means of production would increase the output associated with any given input of labour: of this more will be said later. But poverty might also be relieved by redistribution among the workers of that part of current income appropriated

by the owners of land and capital. The moral foundation of this demand was a crude form of the labour theory of value. John Locke had said:<sup>1</sup>

‘... every man has a property in his own person: this nobody has any right to but himself. The labour of his body, and the work of his hands, we may say, are properly his. Whatsoever then he removes out of the state that nature has provided, and left it in, he hath mixed his labour with, and joined to it something that is his own, and thereby makes it his property.’

Adam Smith had said at the commencement of the chapter on wages in *The Wealth of Nations*: ‘The produce of labour constitutes the natural recompense or wages of labour’. Ricardo had said that goods exchanged in the ratio of their labour content but at values in excess of the wages paid to labour. From this it was an easy step to claim that labour alone produces wealth and is exploited if others establish a claim to part of what is created.

#### THE LABOUR THEORY OF VALUE OF THE CLASSICAL ECONOMISTS

The labour theory of value of the classical economists lent itself to misinterpretation from the way in which it was expressed. The whole temper of their work, however, indicates that it was employed as ‘shorthand’ for the money costs of production, and that they were talking about what we should today call ‘long period normal prices’. No one can escape wholly from the

<sup>1</sup> *Of Civil Government*, Book II, Ch. V, *Works*, 1768 edition, p. 229.

environment of his formative years. To quote Max Beer:<sup>1</sup>

'They were still thinking of domestic industries, farmers, small traders, and independent craftsmen rather than of wage-labour divorced from the mental functions and tools of labour, which is the main characteristic of the factory system . . . It is altogether an absurd belief that an illiterate boy and female worker tending a machine should create new values, while . . . the highest exertions of countless ages of collective human thought and endeavour should be barren of economic values . . . The active agent, then, in the production of wealth is mind, and as it was mainly under the system of private property that the human mind brought about those inventions, discoveries and organisations, the new wealth which they have been yielding takes, therefore, the form of property and capital.'

#### THE EARLY SOCIALISTS' INTERPRETATION

The early socialists however regarded the new capitalists of the industrial revolution as 'mere speculators, cunning money-mongers' coming between the worker and the full product of his labour.

'The means enabling tradesmen to share or take a part of the product of the labour of the poor, is their capital which puts it into their power to furnish materials to the artificers to work on, and to provide them with immediate subsistence, and on that account is supposed to give the tradesmen a just claim to a part of the production of the worksman's hands'.<sup>2</sup>

<sup>1</sup> *History of British Socialism*, Vol. I, 1929, pp. 196–7.

<sup>2</sup> Charles Hall, *Effects of Civilisation*, 1850 edition, p. 57.

Thus it appeared to them just to re-appropriate to the manual labourers that of which they had been robbed. This alone would not have been enough to remove poverty, substantial as the aggregate profits of the period must have been to judge by the architectural beauty of contemporary Bath and London.

The early socialists considered that the replacement of competition by the collective ownership of industry or by producers' co-operative societies would not only serve the end of justice but would also lead to an age of plenty. Reading now through the many schemes which were produced, observing their frequent incompatibility, and reflecting upon the administrative quality of the people who would have tried to operate them, it seems inevitable that had the experiment of collectivisation then taken place the stream of wealth would in all probability have almost dried up. But the contemporary socialists thought that there were forces inherent in collectivism which would widen and deepen it. Is this true? Is there a separate socialist science of economics which besides studying economic problems with moral standards and orders of priority different from those to be expected of the owners of land and property, has in addition a separate and more penetrating logic, more precise and more comprehensive categories of analysis?

Can it be claimed, first, that labour in a socialist society would be more productive? There is little doubt that, at the time when the early socialists were writing, malnutrition, disastrous housing conditions, epidemic disease and illiteracy were keeping down the physical productivity of labour, and that this effect was part of a vicious circle of low wages and over-work. Robert

Owen in New Lanark proved that the circle could be broken, and that wages could rise and labour costs simultaneously fall. In such circumstances, as Marshall argues in the *Principles*,<sup>1</sup> a rise in wages can perpetuate itself. But viciously low wages are not an integral part of a free enterprise society; they characterise the period of the 'take off' from more primitive conditions. There is now no longer, as there was in earlier days, a great difference in health, physique and literacy between the manual worker and the rest of society. It is thus very doubtful if a change to collectivism in an advanced country would now do anything to increase the productivity of labour, unless it took place in circumstances where a dictatorial government could break down many of the justifiable protective powers of the trade unions. It is even more doubtful if what Young called the 'magic of ownership which changes sand to gold' would in the case of *collective* ownership similarly release a flow of energy and devotion. The utmost which might be hoped for is increased willingness on the part of organised labour to co-operate more fully with management, which they might then regard with more confidence. All that need be said to explain the circumstances in which it is possible for wages to rise is to be found in modern economic theory: wages in fact have risen very appreciably since the Industrial Revolution.

Second, are there general advantages which co-operative production possesses over competition? There were indeed many grave defects in early capitalist organisation, notably periodic general unemployment

<sup>1</sup> Alfred Marshall, *The Principles of Economics*, First Edition 1890, last 1920. More than any other, this book is the foundation of economic thought in the English-speaking world.

and a fantastically uneven distribution of income and wealth. The contemporary socialists draw two conclusions: that these evils were an integral part of capitalist organisation and that co-operative production would remove them. Their studies of unemployment led them to develop theories of a general deficiency of purchasing power, dependent upon the uneven distribution of income and upon the very ill-organised financial institutions of the day; the remedies suggested ranged from the purely monetary reforms of Attwood and the 'Banking School' to proposals to substitute labour receipts for money. These remedies were accompanied by a tragic efflorescence of absurdities, like the superiority of spade cultivation and proposals that producers' co-operatives organised by artisans without capital or administrative experience should set up in competition with capitalist production and overthrow it by the display of their superior moral and economic virtues. What very nearly all of these views had in common was the conviction that the evils they denounced were inherent in and irremovable from capitalism and that immediate and spectacular improvement was possible.

(In later passages it is maintained that the poverty and hardships associated with early capitalism, which indeed today recur in countries only now commencing economic growth, if nothing can justify them, can be explained, and both socialist and non-socialist proposals for economic reform discussed, only by the employment of 'orthodox' as contrasted with Marxist techniques of economic analysis.)

### 3. MARXISM

It was this amorphous mass of criticism and speculation which Marx set out to unify and systematise. His work was marked by some enormous advances in realism and clarity. While leaving the philosophers to discuss the general doctrine of dialectical materialism, few would to-day deny the importance of economic events and problems in influencing both history and human thought, and many would agree that class conflict is the greatest of them. Marx argued that class conflict arising out of the poverty of the workers could not be eliminated until productive resources had been developed to a point at which it was possible for *all*, without excessive labour, to share in a civilised life. Recognising that the economic development of the early nineteenth century could not yet support this ideal, he rejected as futile the plans of his predecessors for immediate ameliorisation. Should they attempt to introduce a way of economic life based upon reasonable equality, the universal hardship would either paralyse creative thought and stifle progress or would again give rise to economic conflict as individuals or groups sought to improve their share in an inadequate whole. The moral of this reasoning, which is indeed accepted

by all the countries now under communist government, is that the accumulation of productive capital equipment should be pushed forward as fast as possible in order to lay the foundations of a society free from economic conflict.

It would seem also that, following this same line of thought, one would expect the bitterness of class conflict to become *lessened* as capital accumulated in capitalist countries, and be able to claim as a triumph for Marxist prediction the outbreak of indigenous proletarian and peasant revolutions in backward countries like Tsarist Russia and China, and their improbability in Britain or the USA after the second half of the nineteenth century. But this Marx denied, holding that the productive forces which capitalism developed could not, in the nature of things, bring about an appreciable improvement in working-class standards, and hence a lessening of the class struggle.

He was a prisoner of his system of thought. The dialectical process necessitated that the conflict of forces set up by the emergence of capitalism (itself the synthesis of an earlier conflict) could not be resolved within the system which created them, only by the creation of a new system, a new synthesis. Science was, for Marx, the capacity to understand the determinate process of history according to his own rules. Therefore it was impossible for him to admit that conflict could do anything but become intensified within the economic system which created it. He thus *had* to find proof that things could not improve.

Unless all the economic history of the last century is a myth, Marx has, of course, been proved wrong. By what process of reasoning does he support his con-

clusions? It is here that his version of the labour theory of value becomes central to the argument.

#### THE LABOUR THEORY OF VALUE

The basic thesis of this essay is that nearly all the reactionary and erroneous elements in Marxism originate in the labour theory of value. In the first volume of *Capital* Marx states, quite unambiguously, that goods exchange in the ratio of the socially necessary labour time they contain. He begins by defining exchange value as the ratio in which goods exchange, and saying that it would therefore seem that as the goods which are exchanged are different in their uses it would appear that *intrinsic* value could not exist.<sup>1</sup> But this is not so; if goods exchange in the long run in a given ratio there must be something, common to both, the proportions of which 'value-creating' substance in either determines the ratio of exchange.<sup>2</sup>

It should be noted that the argument has already, even at this initial stage, fallen into error: the necessity

<sup>1</sup> *Capital*, Vol. I, Ch. 1, Eden and Cedar Paul translation, Everyman edition, p. 4. All references to Vol. I of *Capital* will be to this edition. 'Exchange-value shows itself primarily as the quantitative ratio, the proportion, in which use-values of one kind are exchanged for use-values of another kind . . . an exchange-value immanent in commodities (intrinsic value) would consequently appear to be a contradiction in terms.'

<sup>2</sup> *Ibid.*, p. 5. 'Let us look into this matter more clearly . . . For instance our equation may read: one quarter of wheat = x cwt. of iron. What does this equation mean? It tells us that in two different things, namely in one quarter of wheat and x cwt. of iron, there exists in equal quantities something common to both. They are, therefore, equal to a third something, which differs in essence from them both. Each of them, in so far as it is exchange value, must be reducible to the third.'

of causation does not imply a unique cause or 'substance'. Modern economic theory shows that prices come to rest where the desire of consumers for the product has carried production to a point at which the payment they are willing to make for those final purchases on the margin of decision is just enough to secure the resources producing the marginal output, in face of the competing demands for their services from consumers of other products. Prices represent a balance between the forces of supply and demand and the ratio between the market value of two commodities merely denotes where the balance has settled in each of the two cases.

To continue:

'When the use-values of commodities are left out of the reckoning, there remains but one property common to them all, that of being products of labour . . . abstract human labour . . . A use-value of a good (a useful article) has value solely because abstract human labour has been embodied or materialised in it. How are we to measure this value? In terms of this quantity of "value-creating" substance it contains—the quantity of labour.'<sup>1</sup>

Now this is manifestly wrong: in a competitive system goods do not settle down to exchange in a ratio determined wholly by their relative labour content, but in a ratio determined, on the side of supply, by their relative money costs of production, which include payments for the use of both land and capital. The proportions in which land and capital are employed,

<sup>1</sup> *Ibid.*, pp. 6 and 7.

relative to labour, vary very considerably between different industries: thus the cost and price ratio is not the same as the labour ratio. Indeed Marx himself had ultimately to come to the same conclusion. The evidence is in the posthumous papers edited by Friedrich Engels in the third volume of *Capital*. If goods were to exchange at their 'values' as defined in Volume I the rate of profit would be different in different branches of industry and commerce. But here in Volume III Marx says:

'There is no doubt that aside from unessential, accidental and mutually compensating distinctions, a difference in the average rate of profit of the different lines of industry does not exist and could not exist without abolishing the entire system of capitalist production.'<sup>1</sup>

Goods therefore are admitted to exchange in the ratio of their money costs of production, what Marx terms their 'production prices', and not at their labour values.<sup>2</sup>

What then does Marx mean by 'value' if not 'normal market price'? Whether he means it as a measurement of the human costs of production, or as a basis for

<sup>1</sup> Vol. III, Kerr Edition, p. 181.

<sup>2</sup> Unhappily one cannot excuse Marx for this inconsistency by following H. B. Parkes, *Marxism: a Post Mortem* (1939), when he says '... when Marx came to write the third volume of *Das Kapital* he found that some of the theories which he had advanced in the first volume were inapplicable . . .', the inference being that death overtook him before he had time to admit his mistakes or to rectify them. This view has been expressed frequently. But his editor, Engels, in the preface to Vol. III (p. 11), states that the first draft was completed before Vol. I was published.

estimating the exploitation of the worker (see the next section), or whether its significance is indeed mystical, is not our concern here. The point is that he used the concept as if it was really an explanation of how prices and profits were determined and thus a guide to the workings of a capitalist society, in the arguments in which he predicted disaster. And he seems to have continued to use it even after he knew that its original meaning could not be sustained.

#### THE THEORY OF EXPLOITATION

The key to Marx's expectation of progressively deepening capitalist crises lies in his adherence to the fallacy that, although growing productivity may increase the amount of goods produced by one hour's labour, it cannot increase the value of output.

'In equal spaces of time the same labour always generates equal quantities of value, however much the productive power may vary. But in unequal spaces of time then the same amount of labour generates varying amounts of use-value; more when productive power rises, less when it falls.'<sup>1</sup>

To see how this argument influences Marx's predictions concerning the future course of profits one must follow through his proof of economic exploitation. If the value of goods is 'determined' by the socially necessary labour time embodied in them, and they exchange at their 'value' (they do *not*, and, as we have seen, Marx knew it, though he never explicitly disclaimed the analysis of Volume I of *Capital* summarised

<sup>1</sup> Vol. I, *op. cit.*, p. 16.

above), how can profits be made? Only by buying labour-power – the value-creating substance – at its own value, which depends upon the labour-time embodied in the goods which the basic minimum of wages will buy, and working the labourer for a longer time than that required to re-produce his wages. This is the basis of Marx's formula for 'exploitation': it is measured by the ratio of labour hours worked to the labour hours required to produce wage-goods; it is the difference between the 'value' of the product and the 'value' of labour. For Marx it determines the quantity of profit which can be obtained: given the size of the labour force and the ratio of exploitation, profits can be increased no more. Can this ratio be altered? To answer this question requires an examination of Marx's theory of wages, or rather a search for it, because a consistent theory is not to be found anywhere in his works. He begins with a Ricardian 'cost of subsistence' theory: in its original form this is not a theory of wages so much as an explanation of population trends in a primitive society, because it contains no explanation of the demand for labour. But in this form it has a physiological foundation, the minimum beneath which population declines. Marx, however, abandons this in favour of a wage theory based on 'conventional necessities' determined by historical circumstances. While this theory has subsequently been of much service to hard-pressed expositors of Marx driven to proving that an automobile is part of the 'cost of subsistence' of the US wage-earner, it makes nonsense of 'subsistence'. But in the explanation of exploitation in Part III of Volume I the subsistence theory of wages is used as if it had a rigid physiological foundation. Thus the ratio

of exploitation can be increased only if inventions reduce the amount of socially necessary labour time embodied in wage-goods, or if the working day is lengthened, or if labour is paid 'less than its value'.

This is the foundation of the argument that profits must decline if fixed capital increases: profits can arise only out of the exploitation of labour, *not* out of the possession of capital which adds to the output of industry – because, for Marx, what is added by capital instruments is use-value (what today one would define as an increase in real income) and not the exchange-value (determined by labour time) of which he says profits consist. New inventions may lessen the labour-time embodied in wage-goods but cannot abolish it; the working day has physiological limits: if wages fall too far below subsistence for too many workers for too long, the labour force will vanish. Thus, if fixed capital, which adds nothing to value, goes on growing, and if there is a limit to exploitation, set by the maximum number of labour hours that can be extracted from the labour force, the rate of profit per unit of capital must ultimately fall.

#### THE THEORY OF ACCUMULATION

Why does fixed capital accumulate, if it adds nothing to value or profit? There are two explanations in Marx. One is that the accumulation of capital is inherent in the psychology of capitalism. 'Accumulate, accumulate: that is Moses and all the prophets'. Here he was undoubtedly right: there is a built-in propensity to save and to invest in a free enterprise society, sustained in its earlier stages by the fact that it was (as Keynes has pointed out) the 'way of life' of the Victorian business

world; in later periods it is supported by the ambitions and empire-building of company executives. When the propensity to save outruns the opportunity of investment, disaster follows, as we knew only too well in the 1930s. In the passages in which he advances this view Marx was well in advance of most economists of his day, as he often was when he was employing his remarkable gifts of observation and his powerful historical imagination, and when he was unencumbered by the dialectical process and by the labour theory of value. But, alas, this is not the main Marxist explanation of accumulation. It is as follows.

Capital goods are bought at their value, determined by the socially necessary labour time they contain. All that can be contributed to the aggregate profit of the economy was made by the exploitation of the labour which went to their creation, and reposes with the original employer of the productive labour, who sold the capital instruments at their 'value'. As they wear out they contribute their own value, unaltered, to the value of the product. Why then do capitalists acquire fixed capital?

Because it is *socially necessary* labour time, that is the labour time required on the average, which for Marx determines value. Thus, if a new invention reduces the labour time needed to manufacture a product, the first few firms to instal the new plant will produce in less than the socially necessary labour time and will make abnormally high profits. But nemesis will overtake them since, as the rest of the industry adopts this device, the socially necessary labour time will diminish and the abnormally high profits will vanish. Consequently the entire industry will be left with more fixed capital

than before round its neck, adding nothing to value, and with only the profits they had before, determined (as before) by the number of workers they employ and the degree of exploitation. Only if the goods concerned enter largely into wages, thus increasing the degree of exploitation by cheapening wage-goods, or if technological unemployment created by the invention pushes wages below their 'value', can profits increase.

This is of course a travesty of what takes place in times of technical progress. New inventions will be introduced all the time that the increase in the aggregate value of output is just a little more than the interest charges involved in owning the new machine. Not only is this the view of contemporary economists: it emerges clearly enough in Volumes II and III of *Capital*, when Marx is discussing 'production prices' and explaining that competition establishes equal rates of profit between different industries – which would completely inhibit investment being carried to the point which he insists is inevitable in Volume I.

But the idea that the rate of profit must ultimately decline is based on this error, in so far as it has an analytical foundation and does not emerge from the inner necessities of the dialectic. So is the argument that no benefit can come to the masses out of technical progress and increased productivity. As Marx had himself abandoned a physiological theory of subsistence wages, he had to maintain that wages must be kept down by the pressure of technological unemployment – by the creation of a reserve labour army. Marx assumed that technological unemployment would grow very fast, as new capital replaced labour, sufficiently fast to keep wages from rising, perhaps fast enough to force wages

down. But, as we have seen, the amount of labour-saving investment which would take place in a free enterprise society is much less than he supposed. To use the terminology of modern economists, he argued that investment in new equipment would inevitably be carried up to the point where it added nothing to the value of output, i.e. where its 'marginal product' was zero. This would never be done deliberately; it could occur only by accident, and temporarily. In a world of low wages, where the cheapness of labour sets a curb on innovation, it would never happen at all. Investment would proceed to the point when the estimated marginal product of the new equipment was, allowing for uncertainty, slightly higher than the rate of interest. Once more, the absence of a workable theory of price formation, or a reasonable theory of value, betrayed Marx into obvious error.

Marx thus failed to explain the laws of development of a capitalist society, as he set out to do, because of his failure to explain or understand the productivity of capital and the way in which prices are determined.

#### THE REALISATION OF PROFITS

There is another element in *Capital* which scents out a weak spot in free enterprise societies, and indeed in what was until comparatively recently the accepted economists' explanation of their workings. This is what, in Marxist literature, is known as the 'realisation problem'. If the Volume I explanation of value is to be defended, and yet is seen to conform only very slightly with the realities of the market, it is possible to argue that values 'created' are not always realised; that goods must sometimes be sold below their value because, in

the crudest form of explanation, the workers are too poor to buy the whole of their product and the capitalists are too sated. This argument has the twofold strategic advantage of diverting attention from the weakness of the labour theory of value and of concentrating it on the existence of the frequent and prolonged occasions when free enterprise societies have displayed a crippling deficiency of demand. There are many passages in *Capital* which support this view. For example:

‘the epochs in which capitalist production exerts all its forces are always periods of over-production, because the forces of production can never be utilised beyond the point at which surplus value can not only be produced but also realised: but the sale of commodities, the realisation of the commodity capital and hence also of the surplus value is limited not only by the consumptive requirements of society in general, but by the consumptive requirements of a society in which the great majority are poor and must always remain poor.’<sup>1</sup>

Many Marxist writers, particularly Rosa Luxemburg, have attempted to build an entire critique of free enterprise around this theme but have failed. The reason, paradoxically enough, is that Marx was too good an economist (when he got away from the labour theory of value) to lend support to absurd arguments, like those of Major Douglas and the theorists of social credit, who would prove that a capitalist society can never generate enough demand to sell all its output (thus, by implication, proving that there can have been

<sup>1</sup> *Capital*, Volume II, p. 363.

*no* periods of prosperity, *no* growth or development). Yet because of his misunderstanding of the process of price formation, Marx could not define clearly the circumstances in which demand would be adequate to sustain a high level of economic activity and those in which it would not. Indeed it is only recently, employing the tools of analysis which Marxists despise and reject, that we have been able to do so. In Volume III of *Capital* Marx probably came as near to the truth as anyone before Keynes, but he did not solve the problem: to quote Paul Sweezy, academically the most acceptable exponent of Marx<sup>1</sup> (he has been writing of Lenin and Bukharin),

‘again, like Marx, their demonstration of the tendency to underconsumption is fragmentary and incomplete’.

The major predictions that profits must in the long run decline, that the increase in productivity as capital accumulates will not increase real wages, that the class struggle will become intensified in direct ratio with the accumulation of capital, all rest ultimately upon the labour theory of value.

Moreover, they are all demonstrably wrong, on empirical grounds. It is in those countries where per capita investment is highest that wages are highest, and class conflict is the least violent. The return on capital tends to be somewhat lower in those countries, but for reasons which no Marxist would admit. It is because in underdeveloped countries capital is *scarce* that its

<sup>1</sup> *The Theory of Capitalist Development: Principles of Marxian Political Economy*, 1946, p. 186.

productivity at the margin of production, that is, what a little more of it will add to the value of output, and therefore the share of the value of output it can claim, is so high. As capital becomes more plentiful in relation to the other factors, as more and more essential tasks are mechanised, more rivers bridged, more roads constructed, more land irrigated, its marginal product tends to fall and its market price with it. This change is to the benefit of labour, of which the bargaining power and marginal product increases as it ceases to be the overwhelmingly abundant, 'expendable', partner in production. Faced with undeniable evidence that this has taken place, but refusing to recognise the cause, Marxists have two main escape routes.

The first is to argue that one must have regard to the whole world, and that while the standard of living of the workers has been rising during the last decades in the advanced countries, this is only because they have been sharing in the exploitation of colonial peoples, whose standards have remained stagnant or have indeed declined. Thus, taking the workers of the whole capitalist world together, misery has increased as capitalism has developed.

It is indeed sadly true that increases in the standard of living since the war have nearly all been concentrated on the people of the advanced countries. But, first, it has taken place during a period in which political control over the backward areas of the world by the more developed ones has been rapidly lessening. (Lenin, in *Imperialism*, argued that political control over native peoples was an integral element in their economic exploitation.) Second, a most important factor in slowing down economic progress in the backward

areas has been the crippling speed of population growth – mainly due to recent developments in medical science and organisation. Third, and in direct contrast to Marxist teaching, it is the concentration of investment upon the more advanced countries, to the relative exclusion of the more backward, that accounts for the relatively rising standards of the more advanced.

The relative absence of investment in underdeveloped areas is partly due to growing political risks, but also to the relative satisfaction of world demand for some mineral products and for some plantation crops. European and American investment in backward areas has very seldom been in search of cheap labour to exploit: normally it has developed localised natural resources, taking the low-wage, but inefficient, and often therefore relatively expensive labour as an added handicap.

It is the reverse of this picture, however, the positive reasons for domestic investment in the richer countries, which is most damaging to the Marxist thesis. According to Professor Gunnar Myrdal,<sup>1</sup> one of the most authoritative commentators upon this problem, this investment has resulted very largely from the higher degree of social integration in the advanced countries. In economic terms, ten years of full employment and massive investment have so increased the productivity of labour, and its economic and political bargaining power, that the process has become cumulative. Rising wages stimulate a level of investment designed to secure the maximum economy in the use of increasingly

<sup>1</sup> *An International Economy: Problems and Prospects*, London, 1956; *Economic Theory and Under-developed Regions*, London, 1957.

expensive labour; the growing influence of labour in affairs in general ensures a lesser, but still impressive, investment in social capital.

The second escape route from the *impasse* in which the Marxists have landed themselves is to argue that, while the level of employment in the advanced countries is high and steady by comparison with almost the whole of the period for which records exist, it is primarily due to investment in preparation for war. The argument is that investment must go on unless general economic collapse on the scale of the 1930s is to re-emerge; as profits would be forced down if new productive capital were to be created to compete with existing capital instruments, investment in war industry keeps up the level of investment while not impinging upon profits. Thus capitalist institutions contain within themselves the seeds of war: only by warlike preparations can profits be saved from collapse.

There may be a sinister gleam of truth in this argument – but it depends on drawing a line of demarcation between investment in war material and in capital which is productive and of which the marginal productivity may decline, tending to redistribute income in favour of labour, if its growth outstrips the growth of invention and technology. This line of distinction the Marxists, however, are not entitled to draw: for them capital cannot be productive of 'value' (only use-value), so what modern economists regard as productive capital is, in their view, as sterile and profitless a growth as armaments. The appalling burden of armaments expenditure in the contemporary world is political in its origins, and is no more an essential of capitalism than Chinese aggression in India is an integral part of

Communism. Much, indeed, of the economic activity in western countries is based upon defence and thus may be easier to maintain at a steady level than activity based on productive investment. But, even if interested lobbies are developing their own political defence mechanism to the danger of the world's peace, the whole deplorable situation has its origin in the readiness with which the Russians, twice invaded and devastated since the revolution and hence naturally resentful, have listened to prophecies of the inevitable economic decline of the West based upon the confusion of their economic theorists.

## 4. THE DEADLOCK

Imprisoned in their acceptance of all this nonsense, the communists will not genuinely negotiate with powers whose collapse they await. There is no foundation in economic fact or logic for their belief in the basic instability of the free enterprise world. Nor is there any basis for the belief that the transfer of economic life to public control would liberate productive forces, the employment of which capitalism inhibits. But what is *basic* in Marxist thought, the belief that the capitalism of the mid-nineteenth century was a phase in historical development and not the fixed and final culmination of a process of progressive liberalisation, the belief that it would change as a result of the accumulation of capital and consequent social integration, has obviously been proved to be true. Only the Marxists fail to understand the nature of the change that has occurred. They fail to see it because they refuse to recognise progress they have not created, even if in non-communist lands it is the result of measures basically identical with those they have themselves undertaken. The growth of capital equipment in industry, of social capital in education and transport, and of social amenities, which has lightened the labour and transformed the life of the Soviet citizen, has

similar effects elsewhere. Some would indeed say that the process of ameliorisation has on balance gone much further in the non-communist world, reflecting in a higher standard of living the greater accumulation of capital in the West. This is not a question that can be settled by abstract discussion, but only by observation.

## 5. EASING ECONOMIC TENSION IN THE WESTERN WORLD

A secondary thesis of this essay is that as productivity has increased in free enterprise countries it has led to an obvious and clearly recognisable rise in real income, although for a long time the proportion of the working population that benefited was shamefully small. The essentials of this process can be explained very briefly by taking account of the following two propositions:

(1) Broadly, the price which labour power, land, or capital instruments will fetch in competition with one another depends on what people think a little more of each of them (the 'marginal' unit) will add to, or a little less take from, the value of output.

(2) In a free enterprise society which has grown rapidly from nothing by the constant accumulation of privately-owned capital equipment, there *must* be a built-in disposition to save a lot of income.

It follows from (1) that in a society which is short of developed land or of capital they will be scarce relatively to labour; they will thus be put to those uses where they can add much to the value of output, so their price will be high. In such circumstances, as in India to-day, where the annual increase in population is a curse and not a blessing, another million workers

will add next to nothing to output because all the irrigated land and industrial workplaces are full – so that wages must remain low until capital becomes more plentiful.

It follows from (2) that, as all income is derived from producing goods and services or hiring out land or capital to be so employed, and as output can be divided into consumable goods and services and capital instruments, all income is derived from producing one or the other. If for any reason the amount that people are trying to save, i.e. to receive as income without spending it on consumption, is larger than the sums which are being spent on capital instruments, consumer demand will fall below the level expected by the business men who paid out the incomes; they will therefore revise their plans downwards and incomes will fall, as fewer men are employed. Incomes will thus continue to fall until society is so poor that, in the aggregate, it does not try to save more than is currently being invested in new capital goods. It is this tendency for the propensity to save to run ahead of investment which is the source of the recurrent deficiency of purchasing power which has so often plagued free enterprise societies.

#### THE CAUSES OF POVERTY IN MARX'S DAY

Putting all this together one can depict the world of the early nineteenth century which formed the back-cloth to Marx's thought. Wages were low because capital and land were scarce relatively to labour. Thus the distribution of income was heavily weighted in favour of the owners of land and capital, and because there were many large incomes, a high proportion of

national income was saved. But, with wages so low, only those inventions which replaced a very large amount of labour were worth financing. Thus not only was there not enough investment to keep employment at a high level; what there was was of a kind that created the maximum of technological unemployment. Hence the 'reserve labour army' which Marx *saw* in being and which was an effective check on wages. Against this background it was John Stuart Mill, not Marx, who said he doubted if all the inventions so far introduced had lightened the labour of a single person. This was the world which Marx projected into the future.

Yet already, as the hungry 'forties passed, the picture began to be transformed by the continued growth of capital and the development of transport and free trade which increased the effective supply of land and food for the European countries. In periods of high employment, some effective choice of occupations became possible for a large and growing number of wage earners. New capital equipment, by creating a relative scarcity of labour, increased the bargaining power of wage earners. A general working-class sentiment in favour of taking part of the fruits of progress in the form of more leisure led to a lessened offer of man-hours on the labour market, and to still stronger 'selling'. The gradual improvement was interrupted and sometimes reversed by successive trade depressions, but always something seems to have survived from the progress of the previous period of expansion. It cannot be denied that in the advanced countries of the West the level of real wages has risen very considerably, particularly during the last 20 years. The proportion in which the

national income is shared between labour and the owners of the other productive factors does not seem to have altered very much since reliable figures have been available, but not only have total incomes and real earnings per man-hour increased rapidly, but the ownership of capital has become more widely diffused.

This essay is not a defence of free enterprise as a social institution, but of rational economic reasoning, of the kind which seems indeed to be increasingly used in communist planning. What is important from this point of view is that modern economic techniques can describe and analyse the world which Marx saw, and can describe far better than Marxist economists what determined those conditions and what has happened since.

## 6. WHY THE EARLY SOCIALIST AIMS HAVE NOT BEEN ACHIEVED

### IN THE WEST

The immediate aims of the early socialists were freedom from grinding poverty and intolerable overwork. These ambitions have indeed been achieved for the vast majority of the inhabitants of the advanced countries. What remains as the basis of 'socialism' is, for most western socialists, probably dislike of the conflicts of contemporary economic life, combined with ambitions for a yet higher level of consumption and dislike of social and economic inequality. It is easy enough to see why these sentiments survive.

The high level of investment essential if full employment is to be maintained, real incomes to go on rising, and the working day to continue to shorten, is a process of change and development. Investment means mechanising processes previously done by hand, promoting new techniques, building new industries in new places. If it tends to slant the distribution of income away from the mere ownership of capital as capital accumulates and in the direction of labour, it also tends to emphasise the importance of the innovator and thus to increase the incomes of those who possess skills in finance, management, administration and the calculation of

risk. It tends also to cause the normal industrial unit to grow in size and to become de-humanised. New wants are discovered and popularised, incentives to production come to depend largely upon organised emulation in conspicuous consumption. In fact, while all this makes the ordinary wage-earner richer, it tends to increase his frustration and to alienate him. Certainly it does little to lessen economic or social inequality. Conflict and frustration in economic life survive, as they do in life in general. But they are so much lessened in intensity and so much changed in character that probably few would be prepared to accept a way of life sufficiently simple to allow the creation of the conflict-free (and static) economic life which contemporary skills and equipment could probably provide.

Moreover, the *general* stimulus to economic life provided by high investment, easy finance and government spending can lead to contrasts between areas of prosperity and regions of cumulative contraction. The Pennsylvania coalfields in the USA and the north and north-east areas of Britain suggest the need for government direction to supplement the general drive of the pricing system in the direction of high output. We already know that a free enterprise economy needs an 'employment policy' aimed at determining the general level of investment unless it is periodically to be swamped with involuntary unemployment. Marx foresaw this, but explaining the process and prescribing the cure in intelligible terms was reserved for better-equipped economists. The solution of these and other problems is within the scope of modern economics, but it is first necessary to understand the working of the market system, as Marxists do not, before trying to

amend or supplement it without risking a breakdown in its operation.

#### IN COMMUNIST COUNTRIES

It is common ground with Soviet economists that the stage of 'socialism' through which they are now passing, in which land and capital are collectively owned, wages are paid as incentives to productivity, and scarcity and shortage persist, is not their ultimate objective of a society in which economic life proceeds on the basis of 'from each according to his ability, to each according to his need', without constraint or sanction. This eminently sensible objective, however, can be reached only if, as Marx saw, technology and the accumulation of capital have been carried to a high level and wasteful emulation in consumption abandoned. (These conditions can be defined very neatly by modern economists as existing when the marginal productivity of capital, the marginal utility of income, and the marginal disutility of labour, are all equal at zero.)

It may be said that the fundamental obstacle to the fulfilment of 'pure communism' is that the accumulation of productive and social capital has not yet gone far enough. But there are more practical reasons why this process has not proceeded as fast as it might, why investment is not always in the right place, and why it is not always used to the best advantage, which seem to have their origin in the basic errors of communist economics. Many examples can be found in the companion essays in this volume, but they may be categorised here.

The growth of capital has its foundations in agri-

culture: historically it is only when farming can feed more than those who are engaged in it that economic progress begins. The Russian communists came to power after a breakdown of government so complete, and in face of economic and political chaos so enormous, that they alone had courage to assume control. Invasion and counter-revolution further confounded confusion. When order became sufficiently established, the main economic problem was to find food for the towns. There was a surplus of agricultural workers, and if they could be moved into industry and the food they were consuming moved with them, capital formation could recommence. The more food that could be produced and the less labour used in farming, the faster this process could proceed. The logic of the situation demanded that food – the key to industrialisation – should be dear, and that incentives in the form of purchaseable consumers' goods should be available to the peasants. What in fact took place appears at first to have been a grand error of strategy rather than theory: the land was collectivised and grain was vainly demanded from the regimented peasants at low prices. Soviet agriculture has never fully recovered. Worse, in all areas now under communist control the error, or a close variant of it, seems to have been repeated with identical results. Cuba, with fertile and abundant soil and skilled agriculturists, might have hoped to be the first communist area to escape from crippling food crises; but there also the pattern of shortage and rationing has re-appeared. The basic cause of this failure appears to be the Marxist view that exchange values – which regulate production in the capitalist world – must be rejected by good com-

munists as an illogical and misleading mirage. One deplorable result of doctrinaire Marxism has been that communist agricultural policy has not aided the growth of capital; and because productivity per head in agriculture is low labour is wasted and food shortages are intensified.

Before we inquire whether the impressive growth of communist productive capital is in the 'best place' from the point of view of aiding productivity, or is always used to the best advantage, we must make an important disclaimer. In all countries, communist or other, much investment, and a wide sector of activity involving economic resources, is politically determined. There are no economic criteria by which one can deliver judgement upon the desirability or otherwise of what most of the governments of the world are now spending upon armaments, nor indeed upon education, justice and administration (although the economist can evaluate their *cost* in foregone alternatives if he refers to a rational internal economic system for purposes of comparison.) Now most investment decisions in communist countries are political decisions in the sense that they are undertaken after a synthetic judgement upon their suitability from all angles of social policy. Does this mean that they cannot be subjected to economic criticism?

No. The range of activity which ends with the production of consumers' goods and begins with heavy industry, the fabrication of machine tools and the production of materials, can be judged from two angles. In this field consumers choose individually what they wish to buy, unlike the 'consumers' of defence and justice. Does the organisation of production, employing

the resources available, give them as much as possible of what they want, in the proportions in which they want it? That one can never know. But in a society where the price of goods derives from the interaction of supply and demand, and when supply depends ultimately on the conflicting demands transmitted through the pricing system, consumers 'vote' with their incomes for alternative patterns of production. The prices of capital instruments of one kind and another, the rate of interest that helps to determine which industries can afford them, the price of land, the wages of labour, all derive from the same source. What happens in free enterprise societies is that the results may diverge widely from any kind of 'social optimum' because incomes, particularly those arising from inherited wealth, are unequal, because consumers may be unduly influenced by the interested voices of advertisers, and because monopoly raises costs and prices. These can be, and to an increasing extent are, counteracted by redistributive taxation, by education and by monopoly control. In essence the system is rational if not always just, and is capable of rational explanation.

This rationality Marxist economists deny, claiming that a free enterprise economy is based on price ratios determined by socially necessary labour time, and has nothing to do with use-values. This view is untrue; a free market is wholly based on 'use-values'; upon the relative extent to which demands for different goods are more or less fully satisfied. Obviously 'usefulness', in the sense of satisfaction derived from the consumption or ownership of further supplies of anything, depends on how much of it you have already. Communists also deny that it is rational to impute values to productive

capital instruments because they are not capable of adding to 'value'. But it is wholly illogical for them to deny that they are 'productive' while admitting that they aid labour to produce – particularly when communist economic policy is dominated by capital construction.

#### THE EFFECTIVENESS OF SOVIET INVESTMENT

Thus there are two ways in which communist practice lessens the effectiveness with which capital is employed. Where capital is allocated between industries without using a rate of interest as a rough check on what branches of industry expect capital instruments to add most to output, there is the risk of serious mistakes: doubly serious in an economy still consciously short of capital. And secondly, after industrial plant has been installed, in attempting to check the efficiency of its operation by *quantitative* planning controls based directly on 'quantities of use-values' – planning in terms of yards of cloth or hundreds of bicycles, and rewarding managers when they exceed their plan – they again fall short of rationality as soon as they get away from tons of coal or millions of kilowatts. A target set for blocks of cement in terms of *numbers* gets too many small ones; in terms of *weight* too many big ones. Metal roofing becomes too thin when targets are set in terms of *area*, too much when set in terms of *tons*. Mr Khrushchev, writing in *Pravda* on 2 July, 1959, denounced the factory which concentrated upon the manufacture of massive chandeliers: the chandelier plan was set in *tons*. If Soviet administration were prepared to control output in terms of *value*, i.e. money prices, instructing

factory managers to produce up to the point where any further increase in output would push marginal cost, the specific addition to cost involved in producing the last few items, above the price at which the output could be disposed of, there can be little doubt that the system would gain in rationality. It would be more rational because it would stop production of one set of goods at the point where factors of production were adding to the value of output just about what they would add elsewhere in industry. Thus to the consumer the cost of one thing would reflect the alternatives foregone in its production. As industry develops, as more factories produce joint products that can be distinguished in costing only by taking demand into account, and as decentralisation of economic decision-making proceeds, the rationality and the social significance of a price-guided economy seem to be becoming increasingly recognised.

There has been a significant movement of thought in communist circles concerning the value of economic science for a socialist society. In 1877 Engels said:

‘People will be able to manage things very simply, without the intervention of the famous “value”.’<sup>1</sup>

In 1920 Bucharin could still say:<sup>2</sup>

‘Only in a society where production has an anarchistic character do laws of social life appear as “natural”, “spontaneous” laws, . . . Indeed as soon as we deal with an organised national economy,

<sup>1</sup> *Anti-Duhring*, 1878, p. 340.

<sup>2</sup> Quoted by A. Kaufman in *Soviet Studies*, January 1953.

all the basic "problems" of political economy, such as price, value, profit, etc., simply disappear . . . The end of capitalist and commodity society signifies the end of political economy.'

But by 1943 an article generally supposed to have been written by Stalin said:

'To deny the existence of economic laws under socialism means sliding down to vulgar voluntarism, which exists in the substitution of arbitrariness, accident, chaos, for the orderly process of development of production.'<sup>1</sup>

Since the death of Stalin there has been a steadily growing volume of discussion among Soviet economists of the principles that should be employed in framing economic policy. While they have, on balance, moved much closer to western concepts concerning the importance of framing priorities in the light of consumers' needs, and of finding ways of assessing the extent to which particular types of labour are 'socially necessary', it would be misleading to leave the impression that western 'marginal' analysis has been accepted. All of them keep within the somewhat elastic framework of Marxist phraseology: many of the problems of growth and development with which they are confronted need new concepts and techniques of analysis. As these problems were not considered either by the economists whom Marx denounced or by Marx himself they are free to break new ground without blasphemy, and in many fields, like linear programming, they work on

<sup>2</sup> In *Pod Znamenem marksizma*, Nos. 7-8, quoted by Alec Nove, *The Soviet Economy*, George Allen & Unwin, 1961, p. 268.

closely similar lines to the rest of the world. But, and for this essay this is the significant point, in none of this work, as far as the present writer is aware, is there any new proof of the inevitability of capitalist decline, nor any fresh exposition of the manner in which capitalist societies develop potentialities which owing to the contradictions of capitalism they cannot realise. There is, on the other hand, abundant evidence of growing willingness to accept prices which will clear markets, and to use costs reflecting relative scarcity as significant parameters for economic calculation. As these are the foundations of non-Marxist economics, it follows that the movement is away from belief in the 'contradictions of capitalism.' As the late Professor Joseph Schumpeter says:<sup>1</sup>

'bolshevist economists are bound to discover in the end what Pareto and Barone discovered half a century ago, namely that there is an economic logic that has nothing specifically "capitalist" about it . . . National Income accounting and budgeting techniques are rapidly developing in non-bolshevist countries . . . These techniques and corresponding methods of analysis are still more obviously needed in the Soviet state. Thus these tendencies, born of similar needs, have begun to assert themselves independently in Russia and elsewhere, particularly the United States'.

But if prices *are* a significant guide to 'use-value' – which Marxist theory denies – they operate in the same way in a free enterprise economy. Thus the 'contradictions of capitalism', its alleged tendency to create use-

<sup>1</sup> *History of Economic Analysis*, London, 1961, p. 1,159.

values which it cannot 'realise', are from this angle also seen to vanish. The potentialities for increasing production and for lightening labour which the accumulation of capital equipment creates are utilised as they develop, and form the foundation of the rising standard of living which both the communist and non-communist worlds reveal. In America and Europe the accumulation of new capital tends to absorb rather less of the national economic effort than in Russia, partly because we have more to start with, partly because of superior agricultural efficiency, partly because of more rational accounting. We enjoy its fruits somewhat less than we might, because an uneven distribution of income, even after taxes have been paid (which may be the price we have to pay for progress with widely decentralised decision-making), lessens the social significance of the pricing mechanism; because of monopoly; and because of the difficulty our methods experience in dealing with regional unemployment. Particularly is our enjoyment lessened because we have failed to heed the warning of the great economist, Alfred Marshall, against excessive concern with tasteless personal accumulation. We may indeed be said to maintain our high standard of living by working harder than we really want to, because we have been persuaded by the advertising profession that we are miserable because it is not still higher. All this adds up to a quite impressive admission of the faults of free enterprise economy at its present stage of development. But these are not the faults of which the Marxist economists accuse us. There is no fund of potential material wealth which social change could release. Indeed any move in the direction of greater rationality and wider social responsibility might slow

down the output of material wealth slightly, if we enjoy more fully the leisure we can now afford and allow the claims of justice in the distribution of income to blunt incentives. Having built up the material foundations, we can enjoy a little more socialism if we so desire. Fundamentally, Marx was right in this. But he was wrong in his supposition, based on his projection into the future of the conditions in the early nineteenth century, that the process of growth would be accompanied by falling real wages and growing class conflict; he was wrong in supposing that the fruits of progress would accumulate, unenjoyed, until they were released by revolution. We are driven to repeat the basic thesis that it was the labour theory of value – the transformation of a moral judgement about the distribution of income into an unscientific, inaccurate and unworkable explanation of the manner in which prices and incomes were determined in conditions of free enterprise – which warped and distorted his thinking.

In the communist countries capital accumulation nearly everywhere absorbs a larger share of economic effort. This is partly because they started with much less. It was indeed the more intense class conflict inherent in the earlier stages of economic growth which rendered revolution possible. The social pressures involved in capital accumulation with a low standard of consumption probably do much to explain the dictatorial techniques of communist public administration. A second reason is that the investment target is deliberately set high, partly for reasons of defence policy, partly because of a political decision to favour future generations at the expense of the present; neither of these decisions is capable of *economic* criticism. A third

reason is the inefficiency of the agricultural base, in part due to mistakes in economic policy. A fourth is that a higher level of investment is needed to sustain a given level of output the less efficiently capital instruments are allocated between the industries that need them.

#### THE SURPLUS (OR PROFIT ?) AS A GUIDE TO PLANNING

We have suggested reasons for supposing that communist investment is at a somewhat higher level than it need be. Here the interesting thing is the way in which economic literature in Russia reveals a growing body of what is in essence agreement with the views expressed earlier in this essay. One bridge which can be built between western economic thought and Soviet economic practice concerns the concept of 'profit'. For Marx profit was fundamentally a social category: it represented that part of the output of the economy which the workers did not receive as wages, including interest and the rent of land. But, as we have seen, in his explanation of the reasons why capital is accumulated, he employs a 'differential' profit, which is the reward of the innovator, who pays the market price for labour-power and equipment but succeeds in employing them more productively than his competitors. To the western economist the market prices of land, labour, power and capital are determined on the one hand by what the organisers of production think that their employment at the margin of production will add to the value of output, and on the other by what their owners are willing to take for them. Since there is competition between

employers and a constant search by factor-owners for the most lucrative avenues of employment there is a very strong tendency for these prices to exhaust the value of output, except for the gains which remain with those who undertake the uncertainty associated with production in anticipation of market demand and the temporary gains of the successful innovators. Of course, all sorts of frictions distort the picture: organised or unorganised monopoly, ignorance, lethargy – but profit, it is argued, is in the vast majority of cases evidence of constructive ability in economic organisation. This develops from the basic rationality of the pricing system.

Now this principle appears to be gaining recognition in the Soviet Union. In the August 1962 issue of *Voprosy Ekonomiki* Professor Ye. Liberman published an article proposing the recognition of profits in Soviet economic life as an index of efficiency. He declares, of course, that profits in a socialist society are qualitatively different from those in the capitalist world – and he is wholly entitled to do so because they do not accrue to private persons. (The difference, as was argued before, is a 'moral' one. Personal experience confirms the writer's conviction that one can talk quite freely to communist economists and statisticians about profits provided one calls them 'surplus'.) The article was republished in *Pravda* in September and comments were invited; a lively discussion ensued. This was the under-water portion of the iceberg, of which the part visible to the outside world was Mr Khrushchev's speech in November acknowledging that there might be something in profit as an indication of the efficiency of work at the factory level. Into the details of this discussion it

is not our place to enter.<sup>1</sup> What is significant for this discussion is the tacit admission that the creation of a surplus of 'value' above the normal incomes of the factors of production employed is 'productive' in normal circumstances, i.e. when it does not result from cheating or the use of unfair advantage. Thus a capitalist pricing system, too, is not illogical, contains no mysterious suppression of the powers of production, and can be regarded as a rough representation of social costs and benefits.

<sup>1</sup> Dr Margaret Miller discusses it above, pages 30 to 33.

## 7. IMPLICATIONS FOR EAST-WEST RELATIONS

This change in economic thinking seems to be in conformity with the basic view of Marx that science and theoretical thought in general reflect the material framework of society. The change in the capital structure of Russia (and of Yugoslavia)<sup>1</sup>, alters the background to all social thinking. Would a student of Marx, accepting his fundamental point of view, expect economic ideas to be the same in a backward and an advanced society? Would he not expect some growing similarity of concepts, based upon the reflection of basically identical economic problems, between most advanced societies? Would he not expect a growing divergence between the ideas of European communist economists and those of China, and indeed Albania? An interesting projection of this argument seems to be that the right course for Russia, seeking to bridge the growing gulf between Russian and Chinese policy, would be to *increase*, and not to diminish, economic assistance to the Chinese in their programme of development. A still more challenging one would be recognition of the desirability of the western powers, faced with the even wider gulf between communist and

<sup>1</sup> See the essay by Dr Sirc above.

western concepts, proclaiming themselves willing to aid in the economic development of *all* the under-developed countries, irrespective of their political creeds.

There is no foundation for the belief that capitalist society is bound to collapse, nor for the corollary that an extension of public ownership would by itself automatically improve the standard of living.

In the West, socialist parties base their immediate policies on reforms for which justification may be found in orthodox economics: they have, for all practical purposes, abandoned the fallacy that public ownership automatically solves all economic problems, and regard the case for measures bringing industry into public ownership as relying either upon their moral justification or their administrative superiority.

The communist countries have wasted capital they can hardly afford on preparing for the defence of their regimes against the death throes of the West, or for the occupation of areas laid waste by capitalist collapse. The efficiency of their internal accounting has suffered, as they now appear to realise, by employing accounting techniques which do not allow for the social cost of capital creation, nor for the productivity of capital instruments.

If the communists will go back to what is fundamental in Marx, the insistence that economic freedom can only exist in conditions where capital is plentiful and productivity is high, they will be driven to see that the rising level of productivity in the West *lessens* tension in the world, and that the peaceful development of equipment and education in their own countries is the only permanent foundation on which socialism is

possible. Whether the accumulation of capital under conditions of free enterprise, or of state planning, or of a blend of the two, is to prove the most effective in raising the standard of living and lightening human labour only experience can tell. Marx's attempt to prove theoretically that only one path was possible finds no support in logic or in history. His implication that growing internal conflicts will weaken the advanced capitalist countries has led the communist countries into illusions which have carried them to the brink of disaster. What they see in the western world, and the experience of their own development, must combine to prove to them that they will ultimately be judged by what they can provide as a way of life for their people compared with what the market economies can provide. On this basis co-existence based on healthy emulation is possible.

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